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Committee on State Finance and Taxation.

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STATE OF MARYLAND

CONSTITUTIONAL CONVENTION COMMISSION

FIRST REPORT

OF THE

COMMITTEE ON STATE FINANCE AND TAXATION

August 21, 1966

Maryland Room
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College Park, Md.

RE: CREATION OF DEBT AND EXTENSION OF CREDIT BY THE STATE

I. INTRODUCTION

This report reviews in detail the history and present status of Article III, Section 34, of the present Constitution which imposes certain restrictions on the creation of debt and extension of credit by the State and recommends that the section be entirely rewritten. The present section and the proposed substitute are attached to this report with numbered lines to which this report will refer.

The present Constitution, in Article III, Section 54, and Article XI, Section 7, imposes somewhat similar debt and credit restrictions on the counties and the City of Baltimore respectively. Those provisions are also attached hereto. This report does not deal specifically with Article III, Section 54, and Article XI, Section 7, in the belief that those provisions raise fundamental questions of the relationship of the State to its local subdivisions and are therefore not within this Committee's special province. To the substantial extent, however, that the considerations of fiscal integrity which are at the heart of Article III, Section 34, apply to Article III, Section 54, and Article XI, Section 7, the Committee recommends that this report be considered as stating its views on those sections.

II. BACKGROUND

The predecessors of Section 34 were the product of public reaction against the nearly disastrous extent to which the legislature had loaned the credit of the State to rapidly expanding railroad and canal companies during the period of internal development and westward expansion in the United States from 1820-1850. Extraordinary appropriations were made by the General Assembly to such companies, notably the Chesapeake & Ohio Canal Company and the Baltimore & Ohio Railroad, generally by means of subscription to the companies' securities in order to finance their construction programs. Payment of the appropriation was often by transfer to the corporations of long-term state bonds, issued upon the faith and credit of the State. The corporations were entitled to sell the bonds; they did so, usually at substantial discounts, thus effectively raising needed expansion capital by pledging the credit of the State.

By 1840 almost 15 million dollars in state debt had been incurred in order to make such appropriations. The bubble burst when many of the railroad and canal companies, particularly the Chesapeake & Ohio Canal Company, failed to produce the expected revenues to enable them to pay even the interest on the state bonds. The entire obligation was thrown on the State, which had provided no funds for the purpose. An effort by the General Assembly to pay the State's debts by selling the State's interest in the railroad and canal companies was unsuccessful because purchasers for those investments could not be found. Finally, in 1846, the General Assembly saved the State's credit only by imposing additional real estate and personal property taxes to meet these overdue and

accruing obligations. See Hanna, A Financial History of Maryland (1789-1848), Baltimore, The Johns Hopkins Press (1907), pp. 70-105.

III. THE CONVENTION OF 1851

Article III, Section 22 of the Constitution of 1851 provided:

> "Sec. 22. No debt shall hereafter be contracted by the Legislature, unless such debt shall be authorized by a law providing for the collection of an annual tax or taxes sufficient to pay the interest on such debt as it falls due, and also to discharge the principal thereof, within fifteen years from the time of contracting the same, and the taxes laid for this purpose shall not be repealed or applied to any other object until the said debt and the interest thereon shall be fully discharged, and the amount of debts so contracted and remaining unpaid shall never exceed one hundred thousand dollars. The credit of the State shall not, in any manner, be given or loaned to or in aid of any individual, association or corporation, nor shall the General Assembly have the power, in any mode, to involve the State in the construction of works of Internal Improvement, or in any enterprise which shall involve the faith or credit of the State, or make any appropriations therefor. And they shall not use or appropriate the proceeds of the Internal Improvement companies, or of the State tax now levied or which may hereafter be levied, to pay off the public debt, to any other purpose, until the interest and debt are fully paid, or the sinking fund shall be equal to the amount of the outstanding debt, but the Legislature may, without laying a tax, borrow an amount never to exceed fifty thousand dollars, to meet temporary deficiencies in the Treasury, and may contract debts to any amount that may be necessary for the defense of the State."

Review of the debates of the 1851 Constitutional Convention leaves no doubt that Section 22 was drawn in the wake of the State's acute financial embarrassment because of its wholesale extension of credit to the railroad and canal companies. The debates abound with references to the difficulty of marketing state bonds due to the depressed condition of the State's credit and with elaborate expressions of regret that extraordinary taxes had to be

levied in order to meet the debt, with the result that the present generation was being heavily taxed to pay for the follies of the past. See Debates and Proceedings of the Maryland Reform Convention to Revise the State Constitution (1851), Vol. I, pp. 338-357, 369, 375-379, 395, 411, 414-449, Vol. II, pp. 339-347. These excerpts from the debates are typical:

> "...[N]o gentleman who listens to me this day, entertains a doubt, that, if, at the time we became involved in our present enormous debt, those who contracted it, had been compelled at the same time to provide by taxation for its payment, that debt never would have been created. Does not every man know, that when this system was commenced, it was represented and believed, that the revenues to be derived from our great system of internal improvements -- for great I conceive it to be -- would more than pay the interest on the debt and would open to the State a career of prosperity and success, not easily computed? If gentlemen will look back to the elaborate reports made at the time, and to the constant calculations presented to the public, they will find that every man dreamed that he was about to reach a new El Dorado. Taxation was to exist no longer -- public debt was to become an obsolete idea. These works were to bring upon us a flood-tide of prosperity and advancement, which was to know no ebb, which was to be felt to all time, and throughout all the various interests of the State.
>
> "...And, here we are, at this hour, laboring under this great incubus. Let us prevent its recurrence for the time to come. Is there anything so tempting to individuals, States or communities as the contraction of debt? Do we not all know -- every one of us -- that our judgments will be tempted into flattering speculations, not doubting that, in the course of a few months or years, we may double our ventures? The same feeling enters into States. I desire to guard against all such temptations. Let us say to the Legislature, if you choose to construct public works, we required you, at the same time that you create the debt, to lay such a tax as will pay the interest and the principle; for then, and not otherwise, you will be under a just responsibility to your constituents." Vol. I, pp. 343, 345.

Although there was virtual unanimity among the delegates as to the necessity for imposing some restrictions on the power of the legislature to contract public indebtedness, a substantial number of delegates appear to have been opposed to an absolute bar against the loan of the State's credit to "works of internal improvement." A leader of this group, Thomas Donaldson of Anne Arundel County, is reported as follows:

> "Mr. D. said, that no man could be more opposed than himself to wild schemes of internal improvement. He repeated, that he would not advocate the imposition of taxes, for the purpose of making such expenditures. It was better, in general, to leave such undertakings to private capital and enterprise. But he could not consent to deprive the State of the power to use her own surplus receipts hereafter, in the manner which might, at the time, be most conducive to her prosperity. Gentlemen ought not to let themselves be frighted from their propriety, by the alarming apprehensions which had been indulged, in regard to this subject. It was the part of statesmen to restrict a power, so as to prevent its abuse; but not to destroy the power, if, under proper guards, it could be used beneficially." Id. at 343.

A majority of the delegates, however, their attention fixed on the sorry experience of the State in aid of the railroad and canal companies, wrote into the Constitution the prohibitions against (1) the extension of the State's credit to <u>any</u> individual, association or corporation, (2) the involvement of the State in the construction of works of internal improvement and (3) the granting of aid thereto which involves the faith or credit of the State. The dominant spirit which guided the delegates on this aspect of their deliberation was captured in this observation by a contemporary commentator:

> "The twentieth and twenty-second sections, prohibiting the contracting of Public Dept, or the loan of the credit of the State, by the Legislature, will, it is

> to be hoped, prevent her fair name from being again tarnished, as it has been, by a failure to meet her pecuniary obligation to creditors at home and abroad. Honor, as well in a State as in an individual, ought to be as zealously guarded as Liberty." Hinkley, Constitution of Maryland (John Murphy & Co. 1858). p.79.

IV. THE CONVENTION OF 1867

Article III, Section 22 of the 1851 Constitution, unchanged in any significant respect, became Article III, Section 33 of the 1864 Constitution. The Constitutional Convention of 1867 added the following proviso to the section's prohibition against aiding "works of internal improvement":

> "except in aid of the construction of works of internal improvement in the counties of St. Mary's, Charles and Calvert, which have had no direct advantage from such works, as have been heretofore aided by the State; and provided, that such aid, advances, or appropriation, shall not exceed in the aggregate the sum of five hundred thousand dollars." (Lines 13-17 of the present section.)

This exemption appears to have been added to the section in recognition of the fact that the various railroads and canals which had been the beneficiaries of substantial State aid during the 1830's and 1840's were not of direct benefit to the named Southern Maryland counties whose citizens had, nonetheless, been forced to bear their share of the tax burden necessary to pay off the state debt incurred on account of such state aid. The exemption permitted such assistance in these counties to the dollar amount mentioned. See Perlman, Debates of the Maryland Constitutional Convention of 1867, (1923), pp. 270, 279; Proceedings of the State Convention of Maryland to Frame a New Constitution, (1867), p. 346.

V. SUBSEQUENT AMENDMENTS

In 1924 the General Assembly passed and the voters ratified (Acts 1924, ch. 327, ratified 11/4/24) The Veterans Bonus Amendment. The amendment, lines 32-40 of the present section, was designed to remove the prohibition felt to exist against pledging the credit of the State to raise money for a veterans' bonus. It will be noted that any bonus bill was made subject to referendum.

In 1960 an amendment (Acts 1959, Ch. 234, ratified 11/8/60) struck from the section the $50,000.00 limit on borrowing for temporary deficiencies and replaced it with lines 22-32 of the present section permitting tax anticipation borrowing and enabling the state treasurer to meet temporary emergencies.

VI. THE CASE LAW

A. "Debt" within the Meaning of Section 34.

Inquiry must begin with Baltimore v. Gill, 31 Md. 375 (1869) in which the Court of Appeals was called upon to interpret the meaning of "debt" in Article XI, Section 7 of the Constitution which, in language closely paralleling that of Article III, Section 34, provided that:

> "...[N]o debt (except as hereinafter excepted), shall be created by the Mayor and City Council of Baltimore; nor shall the credit of the Mayor and City Council of Baltimore be given, or loaned to, or in aid of any individual, association, or corporation; nor shall the Mayor and City Council of Baltimore have the power to involve the City of Baltimore in the construction of works of internal improvement, nor in granting any aid thereto, which shall involve the faith and credit of the city, nor make any appropriation therefor, unless such debt or credit be authorized by [enumeration of requirements]...."

An ordinance authorized the city to raise one million dollars by the hypothecation of city stock in the Baltimore & Ohio Railroad

and to invest the money in mortgage bonds of the Western Maryland Railway Company. The ordinance further provided that the lenders of the money to the city were to look exclusively to the pledged B & O stock, and not to the general credit of the city, for repayment. A taxpayer's suit attacked the ordinance as the creation of a "debt," the lending of the city's credit to a private corporation and the involvement of the city "in the construction of works of internal improvement," without compliance with the procedural requirements of Section 7. In striking down the ordinance the court rejected the argument that because the parties furnishing the money to the city could look only to the stock pledged, and not to the city's general credit, for repayment, no "debt" was created in the constitutional sense. The mere borrowing of money by the city upon the pledge of a specific part of its property, the B & O stock, was sufficient to create a "debt" within the meaning of Section 7. To the Court, the "plain intent" of Section 7 was:

> "To restrain the municipal government of Baltimore from borrowing money, except for the purposes and in the manner prescribed, either upon the general credit of the city, or by a pledge of its revenues or assets; thereby creating a debt, and imposing additional burdens upon the citizens, which may directly or indirectly involve increased taxation." 31 Md. at 390.

In Wyatt v. State Roads Commission, 175 Md. 258 (1938), the court decided that no state "debt" was created within the meaning of Section 34 by (a) the issuance of revenue bonds to finance construction of the Susquehanna River Bridge where both the authorizing statute and the form of bond expressly provided that the bonds did not constitute a debt or obligation of the State, or (b) the Commission's undertaking, in the trust agreement securing the bonds,

to maintain the bridge. As to the validity of revenue bond financing under Section 34 the court said:

> "Whatever elements of contract by the State, or debt, might be thought to exist in the arrangement, clearly, so far as the cost of construction is concerned, there is no contract to add to the burden of the taxpayers of the State present or future, none to pay anything out of taxes, and no debt incurred for which taxes could be levied. And that is the one kind of debt with which the constitutional clause deals." 175 Md. at 265.

Distinguishing Gill, the court said:

> "The case is not one in which property or income already existing and owned by the State is to be applied to repayment of the cost. The special fund of tolls to be created is an entirely new one, to be borne of the subscriptions to the bonds. By means of the grant of tolls the State is to acquire at once new public highways. The case of Mayor, etc., of Baltimore v. Gill, 31 Md. 375, is cited as an authority for a conclusion that the issue of the bonds would constitute the contracting of a debt for which taxes should be provided under the constitutional clause. It was a case in which stock previously owned was to be pledged to raise money for an investment in railroad stock, but pledged with a stipulation that the lenders should look to the pledged stock alone for repayment, and the pledge was made without compliance with constitutional requirements for creation of a municipal debt. The court decided that the pledge of the existing property was indistinguishable, within the purview of the applicable constitutional clause, from a pledge of credit, and held it the creation of a debt." Id. at 266.

The court decided that construction of Section 34 to prohibit the financing plan in question would improperly extend the constitutional prohibition and usurp the legislative function, especially where such "self-liquidating arrangements to procure new improvements" had been long and widely approved.

The court held that the Commission's covenant to maintain the bridge likewise did not constitute the contracting of a debt on grounds that the promised maintenance was of state property:

"The Constitution does not prohibit all burdens or require all contracts of the State, to be accompanied by laws for levies of taxes to meet them. It deals with burdens of a kind. And an undertaking to pay undetermined, undeterminable, amounts of the cost of maintenance, repair, and operation in the future from day to day, month to month, and year to year, as need arises, if it can be classed as containing an element of debt at all, is not one for which taxes to pay interest and principal, and to pay the principal completely in fifteen years, might be provided in a tax law. There can be no principal and interest in such a contract obligation. . . .

"Whatever debt there might be, would be a debt of the future, and the contract would fall in with the distinction between a debt and a contract to incur future debts. According to all decisions known to us, even if ascertained amounts are now agreed to be paid in the future, as, for instance, rentals, this would not be the contracting of a debt in the constitutional sense. . . ." Id. at 268.

In Castle Farms Dairy Stores v. Lexington Market Authority, 193 Md. 472 (1949), the statute creating the Lexington Market Authority and providing financing for reconstruction of the market was held constitutional under Article XI, Section 7, supra. The statute provided that revenue bonds to be issued by the Authority were not to constitute a debt of the city or a pledge of its faith and credit and that the market property could not be conveyed as security for the bonds. Market property to be conveyed by the city to the Authority was to be made inalienable by the Authority and not subject to attachment for the Authority's debts. Protesting taxpayers argued that, under Gill, conveyance to the Authority of the existing market, a revenue producing property, constituted creation of a "debt." The court held that, even assuming taxpayers' reading of Gill was correct, the argument failed because "(a) the existing market has not been revenue producing but has been operated at a loss, and (b) it is not to be turned over to the Authority

without compensation, but is to be sold for a presumably fair price." 193 Md. at 483-84.

B. "Credit" within the Meaning of Section 34.

In Baltimore & Drum Point Railroad Co. v. Pumphrey, 74 Md. 86 (1891), the court held that where the General Assembly authorized the commissioners of Anne Arundel County to subscribe to stock in a railroad and to issue to the railroad in payment of the subscription negotiable county bonds in the amount of the subscription, a loan of the county's credit had taken place and compliance with the procedural requirements of Article III, Section 54 was necessary. The court said:

> "The primary object of this subscription, and the issue of bonds therefor, was to enable the railroad company to avail itself of the credit of the county to raise funds with which to prosecute its works; and it was therefore a loan of the credit of the county, in a constitutional sense, that the bonds were to be issued upon the subscription . . . ." 74 Md. 86, at 111-12.

In Johns Hopkins University v. Williams, 199 Md. 382 (1951), the court upheld, against attack as a gift or loan of the State's credit, a statute providing for the issuance of state bonds in the amount of $1,500,000.00, the net proceeds of which were to be paid the University for construction of a new engineering building. It was argued to the court that no distinction of constitutional proportions existed between the turning over of county bonds to a railroad to exchange for its stock, construed as a loan of credit in Pumphrey, and selling bonds and giving the proceeds to a corporation. But the court held that:

> "Cash is not credit. Credit is sometimes a means of procuring cash, but the word is never used to describe a gift of cash. There is no prohibition in the Constitution against making appropriations to private institutions, provided the purpose is public, or semi-

> public, and thousands and thousands of dollars are appropriated out of the annual receipts every year. If the State should have a balance of a million and a half in its treasury from annual receipts, there could be no constitutional objection to its giving this amount to the Johns Hopkins University for the purpose of constructing an engineering building. If the State does not have this amount available, but borrows it and then gives the cash to the University, which it is attempting to do, it is not giving or loaning its credit to, or in aid of, the University--it is using its credit with banking institutions to borrow the money, and it is giving the University its cash. What the Legislature of 1951 did by Chapter 414 was not to do by indirection what was forbidden to be done directly--it was to do something entirely different, something not prohibited, something not within the purpose of the constitutional prohibition, not within its wording, and not within its previous long-continued interpretation."

The court made absolutely clear that its construction of Section 34 to permit the proposed bond issue was influenced by the "unquestionable historical reasons" for Section 34, viz., "to curb the reckless and improvident investment of public funds in aid of railroads and canals, promoted by private corporations, organized primarily for profit to their stockholders, although they might eventually serve a public purpose" and by the long Maryland history of the issuance of state bonds and appropriation of their proceeds to nonprofit educational institutions.

In Melvin v. Anne Arundel County, 199 Md. 402 (1951), decided the same day, the court, citing the authority of the Johns Hopkins case, held that the issuance of county bonds, the proceeds of which were to be given to a non-stock, nonprofit general hospital in the county, was not the gift or loaning of credit to an association or corporation within the meaning of Article III, Section 54, but was a gift of cash.

C. "Works of Internal Improvement."

In Bonsal v. Yellott, 100 Md. 481 (1905), the court held that a state grant to counties for highway construction was not the

involvement of the State "in the construction of works of internal improvement in violation of Section 34." The court's exhaustive review of the historical setting and purposes of Section 34 led it to the conclusion that railroads, canals, and "possibly turnpikes," but not public roads, were the "works of internal improvement" which had been the objects of the reckless spending Section 34 was designed to curb. The court said that "the works of internal improvement intended [in Article III, Sections 34 and 54] were such as the State had been connected with or interested in as 'stockholder,' or 'creditor'--such as had driven it to the very verge of bankruptcy and repudiation--and not such as every state government must have, either in its own name or in the names of its 'political agencies, created for the better government of the affairs of the State....'" 100 Md. at 505.

Following Bonsal, facilities which have been held not to be "works of internal improvement" within the meaning of Article III, Sections 34 and 54 are drainage and sewerage systems (Welch v. Coglan, 126 Md. 1 (1915)); a public bridge (Wyatt v. State Roads Commission, supra); a public market (Castle Farms Dairy Stores, Inc. v. Lexington Market Authority, supra); an educational institution (Johns Hopkins University v. Williams, supra); a general hospital (Kelvin v. Board of Commissioners of Anne Arundel County, supra); and an international trade center (Lerch v. Maryland Port Authority, 240 Md. 438 (1965).

D. Recent Developments.

1. The Maryland Port Authority Case.

Within the last year, the Court of Appeals has upheld, against attack as the contracting of a debt by the State without

compliance with the tax and redemption requirements of Section 34, a proposed issue of revenue bonds by the Maryland Port Authority for acquisition and construction of an International Trade Center in the port of Baltimore. Lerch v. Maryland Port Authority, supra. In addition to the normal features of revenue bonds--pledge of the revenues derived from the project constructed with the bond proceeds--the Port Authority issue contained two unique features: (a) the Authority may be required to deposit with the trustee under the trust agreement monies from the Center's general funds which, with the proceeds of the bonds, shall be used to pay the cost of the Center, and (b) the Center is to be conveyed to the trustee as security for the payment of the principal of and interest on the bonds, with power to sell the Center upon default.

As to the deposit feature of the proposed issue, the court, after noting that the amount presently budgeted was an insignificant part of the Authority's general funds and expressing the assumption that any additional sums committed would bear a reasonable relationship to the Authority's available cash resources, said:

> "As was pointed out in Johns Hopkins, supra, cash is not credit and the use of cash does not create a debt. Cash is property, but the present expenditure of cash from current revenues does not create a situation such as existed in Gill whereby valuable existing property of the State may be lost. In Gill, the pledging of the City's valuable and income-producing stock was an obvious subterfuge whereby, in effect, although not in terms, the City's credit was involved. A sale of the stock, on default, could have resulted in increased taxation. In Wyatt, there was no provision for the assignment or conveyance of any State property for the revenue bonds, but, in discussing Gill, we referred to the fact that, there, valuable stock owned by the City was to be pledged for securities of a railroad under construction. In Castle Farms, the land on which the old market stood

was to be conveyed to the Market Authority, but we pointed out, inter alia, that the existing market had not been revenue producing and had been operated at a loss.

> The majority view in other jurisdictions is in accord with Gill, that when existing valuable, income-producing property of the political subdivision is mortgaged as security for the payment of bonds used to finance the construction of a facility, a debt is created . . . . Here, however, we have, not the pledge of existing property, but only the use of cash for the construction of the proposed facility from the Authority's general funds. As in Castle Farms, no burden of taxation on future generations by the future sale of existing property is involved. 'There is no prohibition in the Constitution against making appropriations to private institutions, provided the purpose is public, or semi-public, and thousands and thousands of dollars are approriated out of the annual receipts every year.' Johns Hopkins Univ. v. Williams, supra, 197 Md. at 401.
>
> "The present use of cash from current funds is essentially different from the pledge of valuable property the income from which, as in Gill, may have a direct bearing on the tax rate. Here, the situation is analogous to the appropriation of current funds of the State in the construction of access highways to bridges of the State Roads Commission. While it is true that the highways, when built, remain the property of the State, they are valueless without the bridge to which they lead, as was the old market in Castle Farms. For example, without the construction of the Chesapeake Bay Bridge, the dual highway which was built with State money as access to the bridge would lead only to empty shore." Id. at 457-59.

As to the pledge of the Center, when built, as additional security for the bonds, the court found that the plan "will not jeopardize any property of the State which now exists. If there is a default in the bonds and the Center is sold for the benefit of the bondholders, the State will lose nothing which it now has. The future burden on the taxpayers will be no greater than if the Center had never been built." In concluding that neither novel feature of the proposed issue violated Article 34, the court stressed "the import of our prior opinions on the purpose and interpretation" of Section 34 and the "limited effect" of the two features under attack.

2. The State Colleges Case.

In Lacher v. Board of Trustees of the State Colleges, ____ Md. _____ (No. 106 Adv., Sept. Term 1966, decided July 20, 1966), the Court of Appeals held that the issuance, to finance construction of new state college dormitories, of long-term revenue bonds secured in part by a pledge of increases in fees from existing public college housing did not create a "debt" within the meaning of Section 34. To the argument, based on the Gill case, supra, that the proposed financing -- a pledge of revenues from existing buildings -- was the pledge of an "asset" and thus creation of a "debt," the court said:

> "Gill has been limited in its effect by later cases to its precise holding that a pledge or mortgage of existing governmental property creates or constitutes a debt. [citing Wyatt v. State Roads Commission, Lerch v. Maryland Port Authority, Castle Farms Dairy Stores v. Lexington Market Authority, Johns Hopkins Univ. v. Williams, supra] . . .
>
> "Limiting Gill, as have prior cases, as holding no more than that the creating of a lien on existing property to secure a borrowing of money creates a debt by the borrower, we think it is not a bar to a finding that the pledge of non-tax revenues from an existing facility towards the payment of revenue bonds issued by an agency of the State is not in itself the creation of a debt by the State."

The court pointed out that the legislation authorizing the proposed financing expressly declared that the revenue bonds would not constitute a debt of the State, required the bonds to so state, and prohibited the mortgaging of existing state property to secure the bonds. It also rejected, primarily on the authority of Wyatt v. State Roads Commission, supra, the argument that a "debt" was created in the constitutional sense by virtue of the diversion of dormitory fee increases to service the bonds and the consequent use for dormitory maintenance purposes of state tax revenues not now so used:

"The obligation of the State to maintain the buildings at the State Colleges in the future is exactly that it has to maintain any buildings it owns and that of any provident owner of property. It has not agreed with the bondholders or with anyone else to pay any amount in future years to maintain any building. Whether it does maintain them depends on whether the Legislature appropriates the necessary funds, and it cannot be forced to authorize such expenditures. An obligation of this sort is not in our view a debt within the meaning of the Constitution."

3. The St. Mary's College Case.

In a companion case decided the same day, the Court of Appeals held, for the reasons set forth in the State Colleges case, that the financing of new dormitory construction at St. Mary's College by issuance of long-term revenue bonds secured by a pledge of fees from existing dormitories did not create a debt within the meaning of Section 34. Waring v. Board of Trustees of St. Mary's College of Maryland, ____ Md. ____ (No. 48 Adv., Sept. Term 1966, decided July 20, 1966).

4. The Maryland Industrial Development Financing Authority Case.

In 1965, an act of the legislature created the Maryland Industrial Development Financing Authority (MIDFA) and gave it the power to insure mortgage loans secured by industrial projects. Article 41, Sections 266 J to 266 CC, Annotated Code of Maryland (1965 Replacement Volume). The declared purpose of the act is that "a need exists for new and expanded industrial enterprises to provide enlarged opportunities for gainful employment by the people of Maryland and thus to insure the preservation and betterment of the economy . . . in the interest of the public welfare." Pursuant to the act, MIDFA approved an application of a private steel company

for the insurance by the State of the principal and interest payments of a mortgage to be executed by the county commissioners of Washington County in order to finance construction of a steel rolling and fabricating facility for lease to the steel company. A taxpayer's suit challenged the transaction on the grounds, inter alia, that the act and the contemplated transaction violated Article III, Section 34 of the Constitution in that (a) the credit of the State would be given, loaned to or in aid of a private corporation, (b) the State would be involved in the construction of works of internal improvement and in granting aid thereto involving the State's faith and credit, (c) the State would be called upon to make appropriations for works of internal improvement, and (d) a debt would be contracted by pledging the State's faith and credit to insure a mortgage without compliance with the restrictions of Section 34.

In Maryland Industrial Development Financing Authority v. Meadow-Croft, ____ Md. ____ (No. 199 Adv., Sept. Term 1966, decided July 20, 1966), the Court of Appeals held that a section of the act purporting to pledge the full faith and credit of the State in support of the mortgage insurance was misleading because that section was contrary to other sections of the act which limited the State's obligations as insurer of the mortgages, and held that the act must be construed so as not to pledge the full faith and credit of the State. In view of the admitted fact that the act's full faith and credit pledge was felt to be necessary in order to create investor confidence in the insured mortgages, the court's construction severely limits the act's effectiveness.

Although the court had no occasion to decide the important questions arising under Section 34, it did make clear its awareness of the necessity of some restrictions on the extension of state credit:

> "The faith and credit provision of Section 34 of Article III has been substantially unchanged since the adoption of the Constitution of 1851. The clause was inserted in that Constitution to re-establish and preserve the State's credit after a period of deep financial troubles during which Maryland's fiscal standing was seriously affected. . . . Since the adoption of that constitutional provision, as the record below evidences, the credit of the State has been strong and unimpaired. . . . The record shows that for a long period Maryland bonds have been given a triple A rating, the highest, except for two or three years in the 1940's when they were temporarily reduced to double A."

VII. COMMENTARY

A. Introduction.

The Committee believes that Section 34 should be entirely rewritten. The heart of the present section, the provisions requiring each incurred debt to be accompanied by a specific tax exclusively devoted to debt service, limiting maturity to 15 years and prohibiting extension of the State's credit to "any individual, association or corporation" (lines 1-13) was a response to a specific evil -- the reckless commitment of the State's credit to the railroad and canal companies over one hundred years ago. The sweeping language of these prohibitions, read literally, would appear to preclude the State from engaging in such commonplace and essential forms of financing as long-term revenue bond financing -- in which only funds derived from the financed project are pledged to service the "debt" -- or borrowing for the purpose of making grants to private educational institutions or hospitals. To be sure, as the analysis

in Part VI indicates, these prohibitions have been generally construed by the courts against the background of their adoption and the judicial interpretation has generally accommodated the section to modern financing techniques -- but not without a price. Frequent litigation has been essential. The meaning of the words "debt" and "credit," as used in the section, have taken on highly specialized meanings understood only by the initiated. The words of the present section, in short, do not mean what they appear to say. Two of the goals which the Committee has had in mind in redrafting the section, therefore, have been to make it as intelligible as possible to the average citizen and flexible enough clearly to permit the State to employ its credit in ways unforeseen in 1851 and, indeed, unforeseeable today.

The Committee has been extremely sensitive to the fact that the State today enjoys an AAA credit rating, the highest accorded to the bonds of any state or municipality. It met with representatives of the leading banking and investment houses in Maryland and with a representative of Moody's Investors Service, Inc., the agency primarily responsible for rating the State's bonds, in an effort to learn what effect, if any, changes in the section would have on the State's credit rating. It must be emphasized that the basic inquiry was not as to the soundness or unsoundness of particular uses of the State's credit but was directed to the effect on the State's credit rating of changes in its organic law, per se.

Although the views of the banking and investment witnesses were not always unanimous, there was general consensus on certain important points:

1. The State's credit rating would not suffer if the requirement that each loan be supported by a specific tax were abolished, so long as the full faith and credit of the State and the State's unlimited taxing power were permitted to stand behind its general obligation bonds.

2. Some constitutional limitations on the maturities of bond issues are essential in order to maintain the State's credit rating at present levels. It was generally felt that the constitutional limit could be moved from 15 to 25 years without danger to the State's credit rating.

3. Revenue bond financing is necessary and desirable. The constitution should make it clear that revenue bond financing is permissible.

4. While constitutional provisions are relevant to a state's credit rating, the soundness of the State's management of its fiscal affairs in practice is of far greater importance.

B. Specific Recommendations.

1. Elimination of the Specific Tax Requirement. The Committee felt that the requirement that each bond bill be accompanied by a specific tax for debt service should be eliminated. Historically, the requirement has been served by legislative use of the real estate tax and, for all practical purposes, has pre-empted local subdivisions from use of the real estate tax. The Committee believes that, so long as the full taxing power of the State stands behind its general obligation bonds, elimination of the specific tax requirement will not affect the State's credit. The Committee recommends, instead, inclusion of a requirement (lines 8-15 of the

proposed draft) that when the General Assembly does not appropriate sufficient funds for service of a particular debt, the comptroller shall set apart from the first revenues thereafter received applicable to the general fund a sum sufficient to service the debt. This provision has been recommended to the Committee by several of its witnesses. A counterpart is presently in the Constitution of New York State. It is believed that the proposed provision will give needed flexibility to the State's servicing of its debt. Additionally, the proposed draft's requirement of the irrevocable pledge of the State's full faith and credit and unlimited taxing power (lines 3-5 of the proposed draft) makes clear the State's commitment to service of its debt.

2. Clarification of the "Debt" Concept. The Committee believes that the inclusion of lines 5-8 of the proposed draft will make it clear that only general obligation bonds, supported by a pledge of the State's full faith and credit and unlimited taxing power, will be considered a state indebtedness subject to the restrictions of the section.

3. Maturity Limit of 25 Years (lines 15-17 of the proposed draft). The Committee believes that the maturity limit for general obligation bonds can safely be changed to 25 years. Most bond-financed projects have useful lives longer than 15 years, and closer coordination between the useful life of the financed project and the life of the loan would promote greater and desirable flexibility in the establishing of maturity schedules for the bonds in question. The Committee felt that a maturity limitation in excess of 25 years might adversely affect the State's credit rating

and would be too great a shift of financial responsibility for today's progress to future generations.

4. Extension of State's Credit Limited by "Public Purpose"(lines 17-20 of the proposed draft). The Committee believes that a "public purpose" test should be the only limitation on the State's uses of its credit. Such a test rests on an accepted body of Maryland judicial opinion. See, e.g., Johns Hopkins University v. Williams, supra; Melvin v. Anne Arundel County, supra; City of Frostburg v. Jenkins, 215 Md. 9 (1957). In the Frostburg case the court sustained the power of a municipality to issue bonds and devote the proceeds to acquiring a site and contributing to the cost of constructing a building for a private industry in order to encourage industrial development. As to the claim that the venture served no public purpose and was therefore unconstitutional, the court said:

> ". . .It is also recognized that, with due regard to the legislative prerogative, the courts have a duty to determine whether the particular use is within the scope of the constitutional power. Cf. Arnsperger v. Crawford, 101 Md. 247, 252. But in the application of the principle, it is agreed that 'What is a public purpose for which public funds may be expended is not a matter of exact definition; it is almost entirely a matter of general acceptation.' Finan v. M. & C.C. of Cumberland, supra, (p.565). We may add that the line of demarcation is not immutable or incapable of adjustment to changing social and economic conditions that are properly of public and governmental concern. Cf. Green v. Frazier, supra. . . .The Constitution does not guarantee a static condition of society, or write into our basic law the economic doctrine of laissez-faire. So long as the legislation has a substantial relation to the public welfare and can fairly be said to serve a public purpose, it is not the courts' function to strike it down, merely because we fear it may lead to unwise or unfortunate results. We think the legislation in the instant case is not beyond the bounds of legislative power." 215 Md., at 16,19.

It also appears to the Committee that, although the cases recited in Part VI construing present Section 34 have been made to turn on the

definitions of the specific words in the section, the language of the decisions suggests that the results can fairly be explained by the fact that the courts have often applied a "public purpose" test to the financing arrangement under attack.

The Committee desires to stress, however, that it by no means believes that every extension of credit undertaken with apparent legislative sanction would automatically meet the test. Assuming, for example, that a new MIDFA act is passed clearly pledging the State's full faith and credit to a program of mortgage insurance in aid of industrial development, the Committee has serious doubts whether every project which might be said to fall within the broad declared purposes of the present act would, or should, be held to be a "public purpose."

5. The Committee felt that the provisions of the present section permitting limited appropriation for "works of internal improvement" in the three Southern Maryland counties (lines 13-17) and the restrictions on the use of the proceeds of "internal improvement companies" (lines 17-22) no longer have relevance and recommends their deletion.

6. The Committee recommends deletion of lines 22-31 of the present section relating to tax-anticipation borrowing. The committee believes that the proposed draft would clearly permit both tax-anticipation and bond-anticipation borrowing and that it is unnecessary to make specific reference to either in the constitution.

7. The Committee recommends deletion of lines 31-32 of the present section permitting the contracting of debts for

defense of the State. The Committee believes that the provision is superfluous in view of the public purpose test incorporated in the proposed draft.

8. The Committee recommends deletion of lines 32-40 of the present section, the veterans' bonus amendment, on the grounds that it is superfluous in view of the proposed draft and on the further ground that the subject is not of constitutional dimension.

ARTICLE III, SECTION 34 OF THE PRESENT CONSTITUTION

No debt shall be hereafter contracted by the General Assembly unless such debt shall be authorized by a law providing for the collection of an annual tax or taxes sufficient to pay the interest on such debt as it falls due, and also to discharge the principal thereof within fifteen years from the time of contracting the same; and the taxes laid for this purpose shall not be repealed or applied to any other object until the said debt and interest thereon shall be fully discharged. The credit of the State shall not in any manner be given, or loaned to, or in aid of any individual association or corporation; nor shall the General Assembly have the power in any mode to involve the State in the construction of works of internal improvement, nor in granting any aid thereto which shall involve the faith or credit of the State; nor make any appropriation therefor, except in aid of the construction of works of internal improvement in the counties of St. Mary's, Charles and Calvert, which have had no direct advantage from such works as have been heretofore aided by the State; and provided that such aid, advances or appropriations shall not exceed in the aggregate the sum of five hundred thousand dollars. And they shall not use or appropriate the proceeds of the internal improvement companies, or of the State tax, now levied, or which may hereafter be levied, to pay off the public debt (or) to any other purpose until the interest and debt are fully paid or the sinking fund shall be equal to the amount of the outstanding debt; but the General Assembly may authorize the Board of Public Works to direct the State Treasurer to borrow in the name of the State, in anticipation of the collection of taxes, such sum or sums as may be necessary to meet temporary deficiencies in the treasury, to preserve the best interest of the State in the conduct of the various State institutions, departments, bureaus, and agencies during each fiscal year. Subject to the approval of the Board of Public Works and as provided by law, the State Treasurer is authorized to make and sell short-term notes for temporary emergencies, but such notices must only be made to provide for appropriations already made by the General Assembly. The General Assembly may contract debts to any amount that may be necessary for the defense of the State. And provided further that nothing in this section shall be construed to prohibit the raising of funds for the purpose of aiding or compensating in such manner or way as the General Assembly of the State shall deem proper, those citizens of the State who have served, with honor, their Country and State in time of War; provided, however, that such action of the General Assembly shall be effective only when submitted to and approved by a vote of the people of the State at the General Election next following the enactment of such legislation.

PROPOSED SUBSTITUTE FOR ARTICLE III, SECTION 34

The State shall have the power to incur indebtedness for any public purpose in such manner and upon such terms and conditions as the General Assembly may prescribe. All such indebtedness shall be secured by an irrevocable pledge of the full faith and credit and unlimited taxing power of the State; unless the act of the General Assembly purporting to authorize the creation of such indebtedness includes such an irrevocable pledge, the obligation so authorized shall not be considered an indebtedness of the State. If at any time the General Assembly shall fail to appropriate sufficient funds to provide for the timely payment of the interest upon and installments of principal of all indebtedness created on behalf of the State as provided in this section, the comptroller shall set apart from the first revenues thereafter received applicable to the general funds of the State a sum sufficient to pay such interest and installments of principal. All state indebtedness shall mature within twenty-five years from the time when such indebtedness is incurred. The assets or credit of the State shall not in any manner be given or loaned to any individual, association, or corporation unless a public purpose will be served thereby and unless authorized by an act of the General Assembly stating such public purpose.

ARTICLE III, SEC. 54 OF THE PRESENT CONSTITUTION

No County of this State shall contract any debt, or obligation, in the construction of any Railroad, Canal, or other Work of Internal Improvement, nor give, or loan its credit to, or in aid of any association, or corporation, unless authorized by an Act of the General Assembly.

ARTICLE XI, SEC. 7 OF THE PRESENT CONSTITUTION

From and after the adoption of this Constitution, no bonded debt (except as hereinafter excepted), shall be created by the Mayor and City Council of Baltimore unless such bonded debt be authorized by an Act of the General Assembly of Maryland, and by an ordinance of the Mayor and City Council of Baltimore, submitted to the legal voters of the City of Baltimore, at such time and place as may be fixed by said ordinance, and approved by a majority of the votes cast at such time and place; such ordinance shall provide for the discharge of any such debt within the period of forty (40) years from the time of contracting the same; and provided further that nothing contained herein shall in any manner prohibit the Mayor and City Council of Baltimore from creating any debt to the State of Maryland which may be authorized by an Act of the General Assembly of Maryland; but the Mayor and City Council may, temporarily, borrow any amount of money to meet any deficiency in the City Treasury, and may borrow any amount at any time to provide for any emergency arising from the necessity of maintaining the police, or preserving the health, safety and sanitary condition of the City, and may make due and proper arrangements and agreements for the renewal and extension, in whole or in part, of any and all debts and obligations created according to law before the adoption of this Constitution. Provided, however, that the credit of the Mayor and City Council of Baltimore may be given, or loaned to, or in aid of any individual, association or corporation as the same may be authorized from time to time by an Act of the General Assembly of Maryland.

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SECOND REPORT

OF THE

COMMITTEE ON STATE FINANCE AND TAXATION

October 14, 1966

RE: STATE BUDGET -- ARTICLE III, SECTION 52

I. INTRODUCTION

In its consideration of Article III, Section 52 -- the budget provision of the Constitution -- the Committee heard testimony from Messrs. James G. Rennie and James P. Slicher, Director and Deputy Director, respectively, of the Department of Budget and Procurement of the State of Maryland; Mr. Charles L. Benton, Director of Finance, Baltimore City; Mrs. Janet L. Hoffman, Fiscal Advisor to the Baltimore City Council; Mr. John G. Lauber, Director of Finance, Montgomery County; Mr. John A. Donaho, President of John A. Donaho and Associates, Inc., consultants to governments; numerous representatives of the Maryland State Department of Education, including Dr. James A. Sensenbaugh, State Superintendent of Education; and Mr. Milson C. Raver, Executive Secretary of the Maryland State Teachers Association.

II. BACKGROUND

In 1916 Maryland adopted the state executive budget system, now embodied in Article III, Section 52 of the Constitution. It was the first state to do so. Previously, Maryland, in common with her sister

states, had no orderly system of planned public expenditures. The pre-1916 practice was for the governor, pursuant to the command of Article II, Section 19 of the Constitution, to appear before a joint session of the General Assembly and address it on the "conditions of the State," in the course of which he directed the General Assembly's attention to the State's needs and recommended measures required, in his judgment, to meet them. The governor possessed the power to veto items in appropriation bills (Article II, Section 17), but political realities dictated that he exercise the veto sparingly. Furthermore, vetoed items could be reenacted over his veto. In short, the pre-1916 practice vested the effective power to set the fiscal policies of the State in the legislature.

"Appropriations for various purposes were made piece-meal by the General Assembly, each project receiving independent consideration without relation to other claims upon the public purse." McKeldin v. Steedman, 203 Md. 89, 96 (1953). Whatever the practical possibilities, in an earlier day, for state legislators to have a total picture of the State's fiscal operations, by 1916 the growth of the State's machinery made it impossible. Expenditures were made in a haphazard fashion and "logrolling" for pet projects of various legislators was common, with the result that embarrassing deficits occurred in the state treasury. In 1915 alone the treasury showed a deficit of $2,000,000. Furthermore, important state activities and needs were overlooked. See, H. S. Miles, The Maryland Executive Budget System (1942) at pp. 8-9.

The acute need for centralized budget administration became recognized. Shortly after his inauguration, Governor Emerson C.

Harrington transmitted to the General Assembly a report of the Commission on Economy and Efficiency on a budget system, headed by the late Dr. Frank J. Goodnow, President of The Johns Hopkins University, which contained a proposed constitutional amendment. The report summarized the purposes of the amendment as follows:

> 1st. To impose upon the Governor the sole responsibility, within the limits of the Constitution and the provisions of existing law, of presenting to the Legislature a complete and comprehensive statement of the needs and resources of the State, based upon:
>
> a. Estimates made by those applying for State moneys.
>
> b. Evidence brought out at public hearings on those estimates; and
>
> c. Administrative revision by the Governor of all estimates, except those for the Legislature and the Judiciary, and for purposes for which provision has been made by the Constitution or existing law.
>
> 2nd. To make it impossible for the Legislature so to change the plans proposed by the Governor as to produce a deficit; and
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> 3rd. To permit the Legislature to make provision for any purpose not included in the Governor's plan, on the condition that it provide also for the revenue, which the accomplishment of its purpose necessitates.

The proposed amendment was ratified by the people in 1916 and forms the heart of present Section 52 of Article III of the Constitution. The central purpose of the "budget amendment" was to impose upon the governor primary responsibility for controlling the fiscal policies and operations of the State and on the legislature the secondary task of reviewing the governor's proposals and eliminating unnecessary or excessive items it may discover. Initiative in passing supplemental appropriation bills was permitted the legislature only

after the governor's budget has been acted upon and on condition that each supplemental bill be limited to a single purpose and impose a tax sufficient to produce revenue sufficient to pay the appropriation.

For the most part the executive budget system has served its major purpose, preventing deficits, failing to do so only for a brief period during the Depression. See Miles, The Maryland Executive Budget System, supra. But the continued rapid growth in the State's activities prompted new criticism of the State's budget system. The First Interim Report in 1951 of the Commission on Administrative Organization of the State (the Sobeloff Commission) recommended numerous administrative changes and pointed to two defects which directly affected the constitutional provisions themselves:

(a) It recommended discontinuance of the "line-item" budget and its replacement by a "program budget." The Sobeloff Commission found that the mass of itemized detail submitted to the legislature made it virtually impossible for conscientious legislators to grasp the significance of the expenditures they were called upon to analyze on short notice. The Commission advocated a program budget in which expenditures are grouped by services to be performed so that legislators could more easily establish the relationship between a state service and its cost. See The Maryland Budget System, First Interim Report of the Commission on Administrative Organization of the State (1951), pp. 14-24.

(b) The Commission also found that in practice the power granted the governor by Section 52 (5) to amend or supplement the budget prior to final passage "to correct an oversight, provide funds contingent on pending legislation or, in case of an emergency" had

been abused. It found as follows:

> Knowing that frequently a Governor can be persuaded to include items in a supplemental budget which have not been subjected to careful scrutiny by the Budget Director, petitioners for funds may deliberately neglect to make requests in time for inclusion in the initial budget. Furthermore, the Commission has been advised that the supplemental budget has become a bargaining device between the legislature and the executive. It is said that legislators will at times make approval of proposals sponsored by the Governor contingent on his inclusion of items sponsored by them in the supplemental budget. This means that financial and administrative problems get shunted into an area of political controversy for decision without regard to financial soundness. We are convinced that, with adequate advance notice, the Governor can enforce presentation of all budget requests in time for inclusion in his original budget. In the interest of sound budgeting, we urge that he do so. The power will remain, as now, to use the supplemental budget device to correct mechanical errors and to provide for expenditures required by legislation enacted at the current session prior to enactment of the budget. The Maryland Budget System, supra, at pp. 24-25.

Reaction to the first of the Sobeloff Commission proposals touching the constitutional provisions was swift. In 1952 the voters adopted amendments to subsections (4) and (5) of Article III, Section 52 eliminating the requirement that the budget contain an "itemized" estimate of appropriations, requiring only that the appropriations' estimate be "in such form and detail as the governor shall determine or as may be prescribed by law," and permitting the budget bill to be in such "form" and detail as the governor shall determine or as may be prescribed by law. Since adoption of the amendment, a budget by programs has been employed in Maryland. No changes in the Constitution have resulted, however, from the second Sobeloff Commission finding above cited; namely, the abuse of the governor's power to

amend and supplement the budget. As the comments below will indicate, the proposed redraft of Section 52 submitted herewith attempts to provide safeguards against this abuse.

III. THE CASE LAW

In McKeldin v. Steedman, 203 Md. 89 (1953), the Court of Appeals found that the purpose of Section 52 was not only to prevent the General Assembly from so changing the plans of the governor as to produce a deficit, but also to prevent the General Assembly from reaping the benefits of making popular expenditures while foisting upon the governor the distasteful burden of imposing the tax required to pay the cost of such legislation. The General Assembly had enacted the authorization of a bond issue which included a provision for the levy of a tax sufficient to discharge the interest on the debt as it matured and the principal within 15 years in accordance with the requirements of Article III, Section 34. Thus, the bill, which was conceded to be a supplementary appropriation bill, provided for the levy of a tax for the collection of necessary revenues as required by subsection (8) of Section 52 and could not be responsible for a deficit in the treasury. However, another section of the bill added that the governor should include in his annual budget an item for the payment of principal and interest due on the bond issue in each respective year. The tax provided for in the supplementary appropriation bill was not to be levied unless the general funds appropriated in the governor's budget bill were insufficient to discharge the obligations created by the supplementary bill. The Court of Appeals found this device to be contrary to the purposes of Section 52 and held the bill invalid.

Dorsey v. Petrott, 178 Md. 230 (1940), involved an act of the General Assembly creating an agency to be supported by revenues held in a special fund, and providing for a source of such revenues and the manner in which certain disbursements were to be made. The narrow question before the court was whether the act which established the Commission of Fisheries and empowered the Commission to regulate and administer the laws relating to the seafood resources of Tidewater, Maryland constituted a "law making an appropriation." If so, the act could not properly be submitted to referendum under Article XVI, Section 2, for laws making an appropriation for maintenance of such state agencies are not subject to referendum.

The court held that the act did not make an appropriation. Revenues accruing to the treasury from fines and inspection fees were not disbursed by any provision of the act. The act contemplated that for any disbursement from the treasury to be made, an appropriation or supplementary appropriation was necessary. The provision for salaries of the members and employees of the Commission of Fisheries merely fixed the maximum allowable salaries, and an appropriation bill was required to authorize payment of such salaries.[1] Finally, even if the act provided for a disbursement of certain funds which had been paid into the treasury, nevertheless, it would not be a law

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1. There is some inconsistency between the principles enunciated in McKeldin v. Steedman and Dorsey v. Petrott. The court held in McKeldin that the budget amendment prevents the General Assembly from making an appropriation without shouldering the responsibility of imposing the necessary tax. Under the court's decision in Dorsey a general law may provide that certain sums are to be expended for a particular purpose. It then becomes incumbent upon the governor to provide in his budget the appropriation to pay the cost of the general law.

making an appropriation. A bill proposing an act of general legislation is not converted into an appropriation bill simply because it has had engrafted upon it a section making an appropriation. To be an appropriation bill the primary purpose of the bill must be to make an appropriation from the treasury.[2]

Bickel v. Nice, 173 Md. 1 (1937), stands for the proposition that a supplementary appropriation bill may be "considered," but may not be put to a vote before final action is taken on the budget bill. A bill authorizing a bond issue was challenged on the grounds that it was read and referred to the Committee on Finance of the Senate two days before final action was taken on the budget bill. Subsection (8) of Section 52 provides that:

> Neither House shall consider other appropriations until the Budget Bill has been finally acted upon by both Houses.

The court found the bill to be valid. The purpose of the above provision was merely to prevent submission of another appropriation bill to a vote before final action on the budget bill.

IV. RECOMMENDATIONS

The Committee believes that a provision establishing the structure of the State's budget system should remain in the constitution. In large measure, the practical relationship between the executive and legislative branches of the state government can be

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2. Although in relation to the referendum amendment this proposition may be sound, the clear language of Section 52 indicates that no funds may be authorized to be withdrawn from the treasury unless that authorization is embodied in the executive budget or a supplementary bill accompanied by a revenue measure.

determined by the constitutional rights and duties of each branch with respect to the state budget. The Committee's inquiry into the concept and operation of the state budget system has convinced it that the system is fundamentally sound in theory and practice. Its recommendations are designed primarily to improve the system's operation along lines already charted by the Goodnow and Sobeloff commissions while removing unnecessary detail from the constitution.

A complete draft of proposed new Section 52 is attached as an appendix to this report. For ease of reference, however, each subsection of the proposed draft is reproduced below along with the views of the Committee thereon.

Subsection (1). The General Assembly shall not appropriate any money out of the treasury except by a budget bill or a supplementary appropriation bill, as hereinafter provided.

COMMENT:

The Committee has consolidated the requirements of subsections (1) and (2) of present Section 52.

Subsection (2). On the third Wednesday in January in each year (except in the case of a newly elected governor, and then not later than ten days after the convening of the General Assembly), unless such time be extended by the General Assembly, the governor shall submit to the General Assembly a budget for the next ensuing fiscal year. Such budget shall contain a complete and balanced plan, by programs, of proposed expenditures and shall also contain estimated revenues for said fiscal

year, all in such form and detail as the governor shall determine. The budget shall contain an estimate of all appropriations required by this Constitution or by law. It shall show the estimated surplus or deficit of revenues at the end of the preceding year. The budget shall contain such additional information as may be required by law.

COMMENT:

(a) The first sentence in proposed subsection (2) is identical to the first full sentence of present subsection (3) of Section 52. This sentence was amended by Chapter 161 of the Laws of Maryland of 1964 and approved at referendum in November of 1964. Prior to the amendment, the Constitution required the governor to submit the budget within 20 days after the convening of the General Assembly in odd-numbered years and on the first Wednesday in February in even-numbered years. The present amendment was drawn for the purpose of dovetailing with the new requirements relating to annual 70-day sessions of the General Assembly. The Committee sees no need to change the requirement as it now stands unless the Commission decides upon a different plan for holding the annual meetings of the General Assembly.

(b) The second sentence in proposed subsection (2) contains several innovations:

(i) The word "balanced" is inserted before the word "plan" to insure that the budget submitted will, in fact, be a balanced budget. No explicit requirement to this effect is presently in the Constitution although the Constitution might be read, and has been interpreted, to require the submission of a balanced budget.

(ii) The words "by programs" have been inserted after the word "plan." The Committee feels that this change further will implement the recommendation contained in the Sobeloff Commission report which, as pointed out above, strongly recommended substitution of the program budget for the then existing line-item budget. The 1952 amendment to Section 52, enacted pursuant to the Sobeloff report, eliminated the line-item requirement. The present recommendation seeks to carry this important concept one step further and to make it clear that the budget itself, as well as the budget bill, must be constructed by programs.

(iii) The second sentence of new subsection (2) provides that the proposed expenditures and estimated revenues shall be contained in the budget "in such form and detail as the governor shall determine." Existing Section 52 covers this point, in subsection (5), with respect to the budget bill; it does not do so for the budget itself. The proposed language seeks to supply this deficiency.

(c) The balance of the language contained in new subsection (2) seeks to combine in a more general way the various items specified in present subsection (3) of Section 52 (items which must accompany the existing budget) and items specified in present subsection (4) of Section 52 (estimates of all appropriations which must be contained in the budget). The language contained in existing Section 52 which is omitted from the proposed draft is as follows:

(i) With respect to subsection (3):

> Accompanying each Budget shall be a statement showing: (a) the revenues and expenditures for the preceding fiscal year; (b) the current assets, liabilities, reserves and surplus or

> deficit of the State; (c) the debts and funds of the State; (d) an estimate of the State's fiscal condition as of the beginning and end of the preceding year; (e) any explanation the Governor may desire to make as to the important features of the Budget and any suggestions as to methods for reduction or increase of the State's revenue.

(ii) With respect to the submission of appropriations, present subsection (4) states:

> (a) for the General Assembly as certified to the Governor in the manner hereinafter provided; (b) for the Executive Department; (c) for the Judiciary Department as provided by law; (d) to pay and discharge the principal and interest of the debt of the State in conformity with Section 34 of Article 3 of the Constitution, and all laws enacted in pursuance thereof; (e) for the salaries payable by the State and under the Constitution and laws of the State; (f) for the establishment and maintenance throughout the State of a thorough and efficient system of public schools in conformity with Article 8 of the Constitution and with the laws of the State; (g) for such other purposes as are set forth in the Constitution or laws of the State.

In lieu of the above-quoted language, the suggested draft states the following:

> *The budget shall contain an estimate of all appropriations required by this Constitution or by law. It shall show the estimated surplus or deficit of revenues at the end of the preceding fiscal year. The budget shall contain such additional information as may be required by law.*

The Committee believes that it is unnecessary that the constitution contain detailed requirements as to a statement accompanying the budget or as to estimates which must be contained in the budget. The only requirement which the Committee believes to be of constitutional importance is the requirement that the budget show the estimated surplus or deficit of revenues at the end of the preceding fiscal year. The Committee feels that the omitted detail might appropriately be the subject of a comprehensive budget act, should the legislature see fit to enact one.

Subsection (3). The estimates of appropriations for the legislative department, as required by law, certified by the presiding officer of each house, for the judiciary, as required by law, certified by the chief judge of The Superior Court, and for state support to local school systems, as required by law, shall be transmitted to the governor, in such form and at such times as he shall direct, and shall be included in the budget without revision.

COMMENT:

Proposed subsection (3) is intended to replace the last sentences of present subsections (11) and (12), which accord a limited protection against revision by the governor to the estimates for the legislative and judicial departments and "for the public schools." The present provisions read as follows:

> (11) The Governor for the purpose of making up his Budget shall have the power, and it shall be his duty, to require from the proper State officials, including herein all executive

> departments, all executive and administrative offices, bureaus, boards, commissions and agencies, expending or supervising the expenditure of, and all institutions applying for State moneys and appropriations, such itemized estimates and other information, in such form and at such times as he shall direct. The estimates for the Legislative Department, certified by the presiding officer of each House, of the Judiciary, as provided by law, certified by the Comptroller, and for the public schools, as provided by law, shall be transmitted to the Governor, in such form and at such times as he shall direct, and shall be included in the Budget without revision. (Emphasis added.)
>
> (12) The Governor may provide for public hearings on all estimates and may require the attendance at such hearings of representatives of all agencies, and for all institutions applying for State moneys. After such public hearings he may, in his discretion, revise all estimates except those for the legislative and judiciary departments, and for the public schools, as provided by law. (Emphasis added.)

The existing provisions appeared to the Committee to represent some limitation on the governor's control of his budget. For that reason, and because representatives of the Department of Education and the Maryland State Teachers Association strongly urged retention of the existing protection to the Department of Education budget, the Committee made a special study of the background and operation of the existing provisions, especially as they relate to the "estimates . . . for the public schools."

A. Background

It should be made clear at the outset that the protection presently accorded the "estimates for . . . the public schools as provided by law" has never been construed to encompass the entire budget of the State Department of Education. The protection has been

limited only to "those estimates the amount of which is made mandatory by law," i.e., those estimates made pursuant to the laws of Maryland pertaining to education which require "fixed or mathematically calculable expenditures by the State for the public school system." 36 Op. A.G. 110-111. As the attorney general has pointed out:

> To hold that the Department of Education has uncontrolled power over all appropriation for the public school system would give that Department indirect control over the entire State budget. Yet the Governor and the General Assembly are by Section 52 of Article III of the Constitution charged with responsibility for the over-all fiscal program of the State. 36 Op. A.G. 109 at 111 (1951).

In the view of the attorney general in 1951, budget estimates for the following items fell into the so-called "mandatory" category and could not be revised by the governor or the General Assembly:

> Teachers' Retirement System, exclusive of the Administration Expense Fund.
>
> Aid per classroom unit.
>
> Basic aid per pupil.
>
> Equalization Fund.
>
> Part payment of salaries of school officials.
>
> Incentive Fund for buildings.
>
> Education of physically and mentally handicapped children.
>
> State aid to public libraries.

It should also be pointed out that the attorney general further noted:

> Of course, the facts upon which the estimates are based must be correct, and we think the Department of Education ought to be compelled to show their accuracy. 36 Op. A.G. at 112.

In 1964 the General Assembly made the first major revision in the basic state aid to education program since 1921 (1964, Laws of Maryland, chapter 17), significantly altering the statutory formula under which state aid to education is calculated. The basic purposes of the revision were to raise the level of the State's commitment to public education and to reduce disparities in the educational systems among the counties. The primary features of the revised formula are the guarantee to every child in the State of an expenditure of $340.00 for current expense costs, a required local share for each subdivision in an amount equal to 1.228 per cent of the sum of its "adjusted assessed valuation of real property" and its total "net taxable ordinary income" and a guaranteed minimum state contribution for each pupil of $98.00. Other important details of the rather elaborate structure of the state aid formula are set out and explained in Financing Education for Our Times in Maryland, a pamphlet published by the Maryland State Department of Education in May, 1964. The revision does not appear radically to have affected the so-called "mandatory items" not subject to budget revision by the governor or the General Assembly. In testimony before the Committee on June 9, 1966, Dr. Sensenbaugh cited the following budget items as "mandated":

state share of current expense
current expense incentive aid
pupil transportation
incentive fund for school construction
handicapped children

junior colleges

public libraries

public library incentive aid

teachers' retirement system

Although open to some difference in interpretation, the categories mentioned appear to reflect the attorney general's standard -- i.e., estimates for state aid which require fixed or mathematically calculable expenditures by the State for the public school system.

From the point of view of the Committee, several aspects of the relationship of the Department of Education budget to the constitutional provisions here in question seem relevant:

(a) The "mandated items" fall into what may be termed, broadly speaking, expenditures for "operations" -- expenses such as teachers' salaries, classroom construction, textbooks, heat and light for school buildings, and transportation, which more or less directly relate to the education of the child in the classroom -- as opposed to expenditures for "administration." It has apparently never been suggested, for example, that the salary of the state superintendent of schools or other items relating to the internal administration of the Department of Education are "mandated" items.

(b) Under the attorney general's ruling cited above, the legislature effectively controls the practical meaning of the protections to the Department of Education budget afforded by subsections (11) and (12). The legislature not only determines the quantity of state aid but, by controlling the question of whether to require state aid for given budgetary items by a "fixed or mathematically

calculable expenditure," completely determines what shall or shall not be a "mandated" item. Thus, even the protections afforded by subsections (11) and (12) to mandated items would appear to be sharply limited, in theory, at least, by the will of the legislature.

B. Testimony

Representatives of the State Department of Education and the Maryland State Teachers Association strongly urged retention of the existing provision as a guarantee against "political" interference with the school budget. Dr. Sensenbaugh told the Committee that in other states, where revisions of the education budget as submitted is permitted, the education budget does become embroiled in "politics." Mr. Raver considered subsections (11) and (12) "the primary protection which keeps public schools out of politics" and as even more important than the protection against legislative revision which presently appears in Section 52 (6) and which the Committee has recommended be retained. Representatives of the Department of Budget and Procurement, as well as Mr. Donaho, suggested, with varying degrees of intensity, that the protection be abolished on the ground that it undercut the governor's control of his own budget and thus ran counter to the philosophy of the executive budget system. Mr. Slicher of the Department of Budget and Procurement pointed out that, traditionally, the Department of Education was the largest "reverter" -- i.e., returned the largest percentage of unspent funds to the treasury -- and suggested that this was due in large part to the inability of the budget department to revise education department estimates on the same basis as it revises the estimates of other state agencies.

Much testimony revolved around the extent to which the protection has practical meaning. Initially, there appeared to be significant conflict in the testimony on the question of whether the Department of Budget and Procurement did, in fact, revise some of the estimates, even as to "mandated" items, on which the education budget is based, particularly the estimate as to the anticipated number of pupils for the budgeted school year. The conflict has been seemingly reconciled, however. The true state of affairs would appear to be that the budget department does not hesitate to check those budget items based on estimates by the Department of Education and the Department of Education does not hesitate to correct erroneous estimates pointed out by the budget department analysts. In short, a cooperative atmosphere appears to prevail in which genuine give-and-take occurs. There has been no occasion brought to the attention of the Committee for the Department of Education to insist on the protections of subsections (11) and (12). Education officials testified, however, that the very presence of the protection was in part responsible for the atmosphere of give-and-take in discussions between the budget and education departments.

C. Discussion

The Committee found no hard evidence to indicate that the relative freedom of the Department of Education from "political" interference is due to the protections of subsections (11) and (12). The report of Abraham Flexner and Frank P. Bachman (Public Education in Maryland - A Report to the Maryland Educational Survey Commission, New York, Fifth Edition, 1921), cited to the Committee by Mr. Raver,

contains a strong indictment of political interference in the Maryland school system and recommendations for reform, many of which were incorporated in the extensive reforms of the organization of Maryland's education system passed by the General Assembly in 1916. The report does not, however, make reference to the provisions here in question. The Committee believes that the evil of "political" interference, from a budgetary standpoint, to which sound objection was made in the Flexner-Bachman report was that of "logrolling" for pet educational projects by the legislature. See, Public Education in Maryland, supra, chapters 9 and 12. It will be remembered that legislative "log-rolling" on a more widespread scale was one of the factors which led to the overhauling of the budget system in 1916 and to adoption of the executive budget system. In short, there does not appear to be evidence of "political" manipulation of the education budget by the executive in Maryland for the reason that, prior to the 1916 budget amendment, Maryland had no executive budget system and the governor no effective control of his budget. Since the protections of sub-sections (11) and (12) have been in effect since the initial adoption of the executive budget system, Maryland is simply without experience which would indicate one way or the other whether the feared evils of "political" manipulation by the executive would or would not occur absent those provisions.

Despite the absence of clear evidence that the provisions in question are at all responsible for the absence of "politics" in the public school system, the Committee recognizes that the protection to the education budget has become an important symbol of the freedom

of the public schools from "politics." Since, as pointed out above, the provisions make only a limited inroad into the governor's control of his budget, the Committee feels that, on balance, the substance of the present protection ought to remain in the constitution. The Committee believes, however, that the language of the protection ought more nearly to conform to present practice and to reflect the fact that only items mandated by the General Assembly are protected. Thus, the Committee has substituted the words "as required by law" for the words "as provided by law." The Committee has also substituted the words "estimates . . . for state support to local school systems" for the words "estimates . . . for the public schools." The Committee believes that the proposed substitutions more clearly reflect the nature of those items which have traditionally been "mandated," yet are flexible enough to encompass periodic adjustments in the state aid formula by the legislature.

According to testimony before the Committee, the limited present protections for the estimates of the legislative and judicial branches have worked well as an accommodation between the principle of an executive budget system and the doctrine of separation of powers. The only changes recommended by the Committee are (a) substituting "as required by law" for "as provided by law" to make it clear that only items "mandated" by the General Assembly could not be revised by the governor; and (b) a provision that the estimates for the judiciary be certified by the chief judge of The Superior Court in order to conform with the scheme contemplated by the Committee on the Judiciary Department and recommended in its Fourth Report.

Subsection (4). The governor shall deliver to the presiding officer of each house the budget and a bill for all the proposed appropriations of the budget classified and in such form and detail as he shall determine or as may be prescribed by law. The presiding officer of each house shall promptly cause said bill to be introduced therein, and such bill shall be known as the "budget bill." The governor may, before final action thereon by the General Assembly, amend or supplement the budget bill to correct an oversight, to provide funds contingent on passage of pending legislation or to provide for an emergency. Such amendment or supplement shall be delivered to the presiding officers of both houses, and it shall thereafter become a part of such budget bill as an addition, substitute or modification thereof or any item thereof. Any such amendment shall be accompanied by a statement by the governor explaining the reasons for each budget amendment.

COMMENT:

The first two sentences of proposed subsection (4) reflect the provisions now incorporated in the first sentence of subsection (5) of present Section 52.

The third sentence of proposed subsection (4) is generally taken from the first clause of the second sentence of present subsection (5), with the exception that the present draft eliminates the requirement of present subsection (5) that the governor can supplement

the budget bill only "with the consent of the General Assembly." The Committee feels that such a consent requirement is inconsistent with the executive budget system in which Maryland pioneered and undercuts the governor's primary responsibility for the budget. This view also reflects the testimony of the numerous governmental budget experts who testified before the Committee.

The fourth sentence of proposed subsection (4) is substantially patterned on the last clause of the second sentence of existing subsection (5).

The fifth sentence of proposed subsection (4) is an innovation and is recommended by the Committee as a safeguard against abuse of the governor's power to amend or supplement his budget. The Committee feels that if the governor is required publicly to explain each proposed budget bill amendment, the danger of his attempting to amend it in such a way as to bear no relation to the original document, or of his attempting to make substantial changes on the grounds of "oversight," will be substantially lessened. The Committee is informed that present practice is for the governor to so explain proposed budget bill amendments, but feels that the provision will insure that the practice continues. The Committee believes that this safeguard will meet one of the criticisms of the present system pointed out by the Sobeloff Commission and discussed above.

Subsection (5). The General Assembly shall not amend the budget or the budget bill so as to affect (a) the estimate of revenues therein contained; (b)

the appropriation of sufficient funds to provide for the timely payment of the interest upon and installments of principal of all indebtedness created on behalf of the State as required by Section 34 of Article 3 of the Constitution; (c) the provisions made by the laws of the State for the establishment and maintenance of a system of public schools. The General Assembly may amend the bill by increasing or decreasing the items therein relating to the General Assembly; it may increase the items therein relating to the judiciary. The salary or compensation of any public officer shall not be decreased during his term of office. Except as herein provided, the General Assembly shall not alter the budget bill except to strike out or reduce items therein.

COMMENT:

The present Constitution (Section 52, subsection (6)) states that the General Assembly shall not amend the budget bill in such a way as to affect the following:

(1) Debt service obligations required by Article III, Section 34.

(2) The provisions made by law of the State for the establishment and maintenance of a system of public schools.

(3) The payment of any salaries required to be paid by the State of Maryland by the Constitution.

The first sentence of proposed subsection (5) continues the prohibition against legislative amendment of the budget bill so as

to effect debt service obligations, but does so in language consistent with the new draft of Section 34 proposed by this Committee.

The first sentence of proposed subsection (5) continues the prohibition against legislative amendment so as to affect the provisions made by law for the establishment and maintenance of a system of public schools. This provision is considered to be a significant form of immunization of the public school system from political influence and its retention is strongly urged by representatives of the State Board of Education and the Maryland State Teachers Association.

The first sentence of proposed subsection (5) omits the prohibition against legislative amendment of the budget bill so as to affect salaries required to be paid by the Constitution. The Committee makes this recommendation on the assumption that the new constitution will not provide for specific salaries.

The first sentence of proposed subsection (5) includes a new prohibition against legislative amendment of the budget bill; namely, a prohibition against amendment so as to affect the estimate of revenues contained in the budget bill. Each of the experts who testified before the Committee emphasized the absolute necessity of preventing the General Assembly from tampering with the revenue estimates upon which the governor's budget is predicated. The Committee believes that such a prohibition is vital to the operation of a true executive budget system. It has been informed by the state budget director that, in his long experience, the General Assembly has never amended the revenue estimates, although unsuccessful attempts to do so have occurred. The

Committee feels that the issue is so vital to the executive budget system that a specific prohibition ought to appear in the constitution.

The second sentence of proposed subsection (5) retains the substance of the provisions of existing subsection (6) which permit the General Assembly to amend the budget bill by increasing or diminishing the items relating to the General Assembly and to increase items relating to the judiciary.

The balance of proposed subsection (5) incorporates the substance of the remainder of existing subsection (6) with the exception of the provision in existing subsection (6) relating to the inability of the governor to veto the budget bill. This subject is treated in proposed subsection (6).

Subsection (6). The budget bill shall become law when passed by both houses of the General Assembly. If the budget bill shall not have been finally acted upon by the General Assembly within ten (10) days before the expiration of its regular session, it shall become law in the form and tenor of its original introduction, but this provision shall be inapplicable to any amendment to or supplement to the budget bill made as provided by subsection (4) of this Section 52. In the event the budget bill becomes a law by reason of a failure to act thereon by the General Assembly, any amendments or supplements thereto shall be controlled and governed by subsection (8) hereof relating to supplementary appropriation bills. The budget bill, upon becoming a law, shall not be subject to veto by the governor.

COMMENT:

Proposed subsection (6) is new. A number of experts who testified before the Committee addressed themselves to the problem of legislative delay occasioned by the budget bill. The Committee concluded that legislative work on the budget bill could be completed sooner if the legislature did not engage in seemingly unnecessary detailed analysis and confined itself to the broader aspects of the budget bill. As pointed out above, it was for this very reason that the Sobeloff Commission recommended substitution of the program type budget for the line-item budget.

The Committee feels that the imposition of a time limit on legislative consideration of the budget bill would (a) encourage a broader, program-by-program, analysis by the General Assembly; (b) allow more time for careful legislative consideration of supplemental appropriation bills; and (c) reduce the pressure for a continuing legislative session by promoting the prompter dispatch of legislative business. Accordingly, the Committee recommends that if the budget bill shall not have finally been acted upon by the General Assembly within ten days before expiration of its regular session, it shall become law in the form and tenor of its original introduction. This provision is contained in the first clause of the second sentence of the proposed subsection. To prevent abuse of the time-limit provision by the governor, who could, conceivably, amend his budget one day before it automatically became law and thus obtain provisions not even considered by the General Assembly, the Committee has added the second clause of the second sentence and the entire third sentence which provide, in substance, that any amendment or supplement made to the

budget bill as originally introduced would not automatically become law if the time limit were reached, but would be governed by the proposed subsection (8) relating to supplemental appropriation bills.

The first and last sentences of proposed subsection (6) are recommended on the ground that the constitution should affirmatively state (a) when, in the normal course of events, the budget bill becomes law and (b) that the budget bill is not subject to the governor's veto. The substance of these provisions presently exists in the last clause of existing subsection (6).

Subsection (7). Either house of the General Assembly may require any person in any department, board, branch, bureau or agency of the state government to appear and be heard with respect to any budget bill during the consideration thereof, and the governor or any such person as he shall designate shall have the right to appear for the purpose of explaining the budget bill or any item therein contained.

COMMENT:

Proposed subsection (7) treats in a simplified and unified fashion the subject of the relative rights and duties of the governor and the General Assembly concerning the preparation and hearings on the budget bill currently found in the first sentence of existing subsection (11), the first sentence of existing subsection (12) and existing subsection (7) of Section 52.

The Committee feels that the power and duties granted and imposed on the governor in the first sentence of existing subsection (11) and in the first sentence of existing subsection (12) concerning the

gathering of information from state officials and the holding of public hearings on budget estimates were inherent in the powers of his office and did not require specific statement in the constitution.

The Committee feels that the substance of existing subsection (7), stating the rights and duties of the governor and General Assembly with respect to furnishing explanation and information to the General Assembly, ought to be retained in order to insure that the General Assembly is adequately informed as to the budget bill. It believes it inappropriate, however, to permit the General Assembly to require the governor, personally, to appear before it for this purpose.

Subsection (8). Neither house shall consider other appropriations until the budget bill has become law. Any such appropriation shall be embodied in a separate bill limited to some single work, object or purpose as clearly defined therein, and such bill shall be called a supplementary appropriation bill. Each supplementary appropriation bill, including amendments or supplements to the budget bill which have not become law, shall provide the revenue necessary to pay the appropriation by a tax, direct or indirect, to be levied and collected as shall be directed in said bill, and, in addition, in the case of amendments or supplements provided for by subsection (4) of this section, by funds available therefor in conformity with estimates made by the governor, such estimates being subject to subsection (5) of this section. No supplementary appropriation bill shall become law unless

it be passed in each house by a vote of a majority of the whole number of members elected, and the yeas and nays recorded on its final passage, and such bill shall be presented to the governor as provided in Section 17 of Article 2 of the Constitution, and thereafter all of the provisions of said section shall apply. The powers and rights of the governor and the General Assembly specified in subsection (7) of this section shall apply to any supplementary appropriation bill.

COMMENT:

The proposed subsection continues, in substance, the provisions of present subsection (8) of Section 52 dealing with supplementary appropriation bills.

All of the witnesses who appeared before the Committee were strongly of the opinion that there should be no relaxation of the rule prohibiting any money bill from moving through the General Assembly until after the budget bill has been acted upon. The Committee considered but rejected a suggestion that supplemental appropriation bills be permitted to pass one house prior to enactment of the budget bill. The present draft continues the existing prohibition.

Proposed subsection (8) contains the following substantive provisions which are found in existing subsection (8) of Section 52:

(i) That neither house shall consider other appropriations until the budget has become law.

(ii) That such other appropriations shall be embodied in a

separate bill limited to a single work, object or purpose.

(iii) Such supplementary appropriation bill shall provide the revenues necessary to pay the appropriation.

(iv) That every supplemental appropriation bill shall become law only upon receiving a favorable vote of a majority of the whole number of members of each house elected thereto.

(v) The governor shall have the right to veto any supplementary appropriation bill as provided in present Section 17 of Article 2 of the present Constitution, and all of the provisions thereof shall apply.

Proposed subsection (8) also contains the following additional provisions not found in the present Constitution:

(i) That a supplementary appropriation bill may be funded by surplus or by changing the revenue estimates or by the executive change of previously made revenue estimates. As a matter of fact, the present practice is for the governor to handle a supplementary appropriation bill in this fashion. Accordingly, this proposed change merely allows that which seemingly is not allowed at the present time, but which is done in fact, i.e., to fund a supplementary appropriation bill through a change in revenue estimates.

Proposed subsection (8)-- since it deals with new revenue estimates -- protects these estimates in the same way that the original revenue estimates are protected in subsection (5) of the proposed draft.

The last sentence of proposed subsection (8) is new. It confers on the governor and General Assembly, with respect to supplementary appropriation bills, the powers and rights conferred on each, by proposed subsection (7), with respect to the budget bill. The present Constitution makes no such provision.

Subsection (9). The General Assembly may consider any emergency appropriation at any extraordinary session.

COMMENT:

The proposed subsection is intended to incorporate the substance of the last clause of the second sentence of present subsection (14) of Section 52 in order to make it clear that emergency appropriations may be considered at special sessions of the General Assembly. The first sentence of present subsection (14) has been omitted from the proposed draft. The new document will hopefully contain no inconsistencies; should unforeseen inconsistencies arise, the Committee sees no overriding reason to give primacy to the budget provisions. The first clause of the second sentence of present subsection (14) has been omitted on the ground that its substance has been adequately covered by proposed subsection (5).

Additional Deletions:

Present subsection (9) -- This subsection, relating to the power of the General Assembly to pass laws concerning duties or imposts for inspection purposes as provided in Article I, Section 10 of the federal Constitution, has been deleted on the ground that it is of no practical importance in view of the fact that the State imposes no such duties.

Present subsection (13) -- The subsection has been eliminated because the power to enact laws "necessary and proper" to carry out the constitutional provisions is inherent in the legislature and need not be specified.

Present subsection (15) -- This subsection is in effect a prospective severability clause. The Committee felt that the question of severability of a legislative act is one of legislative intent and should not be presumed by constitutional fiat.

Respectfully submitted,

Committee on State Finance and Taxation

PROPOSED DRAFT OF ARTICLE III, SECTION 52

Subsection (1). The General Assembly shall not appropriate any money out of the treasury except by a budget bill or a supplementary appropriation bill, as hereinafter provided.

Subsection (2). On the third Wednesday in January in each year (except in the case of a newly elected governor, and then not later than ten days after the convening of the General Assembly), unless such time be extended by the General Assembly, the governor shall submit to the General Assembly a budget for the next ensuing fiscal year. Such budget shall contain a complete and balanced plan, by programs, of proposed expenditures and shall also contain estimated revenues for said fiscal year, all in such form and detail as the governor shall determine. The budget shall contain an estimate of all appropriations required by this Constitution or by law. It shall show the estimated surplus or deficit of revenues at the end of the preceding year. The budget shall contain such additional information as may be required by law.

Subsection (3). The estimates of appropriations for the legislative department, as required by law, certified by the presiding officer of each house, for the judiciary, as required by law, certified by the chief

judge of The Superior Court, and for state support to local school systems, as required by law, shall be transmitted to the governor, in such form and at such times as he shall direct, and shall be included in the budget without revision.

Subsection (4). The governor shall deliver to the presiding officer of each house the budget and a bill for all the proposed appropriations of the budget classified and in such form and detail as he shall determine or as may be prescribed by law. The presiding officer of each house shall promptly cause said bill to be introduced therein, and such bill shall be known as the "budget bill." The governor may, before final action thereon by the General Assembly, amend or supplement the budget bill to correct an oversight, to provide funds contingent on passage of pending legislation or to provide for an emergency. Such amendment or supplement shall be delivered to the presiding officers of both houses, and it shall thereafter become a part of such budget bill as an addition, substitute or modification thereof or any item thereof. Any such amendment shall be accompanied by a statement by the governor explaining the reasons for each budget amendment.

Subsection (5). The General Assembly shall not amend the budget or the budget bill so as to affect (a) the estimate of revenues therein contained; (b)

the appropriation of sufficient funds to provide for the timely payment of the interest upon and installments of principal of all indebtedness created on behalf of the State as required by Section 34 of Article 3 of the Constitution; (c) the provisions made by the laws of the State for the establishment and maintenance of a system of public schools. The General Assembly may amend the bill by increasing or decreasing the items therein relating to the General Assembly; it may increase the items therein relating to the judiciary. The salary or compensation of any public officer shall not be decreased during his term of office. Except as herein provided, the General Assembly shall not alter the budget bill except to strike out or reduce items therein.

Subsection (6). The budget bill shall become law when passed by both houses of the General Assembly. If the budget bill shall not have been finally acted upon by the General Assembly within ten (10) days before the expiration of its regular session, it shall become law in the form and tenor of its original introduction, but this provision shall be inapplicable to any amendment to or supplement to the budget bill made as provided by subsection (4) of this Section 52. In the event the budget bill becomes a law by reason of a failure to act thereon by the General Assembly, any amendments or supplements thereto shall be controlled and governed by subsection (8) hereof relating to supplementary appropriation bills. The budget bill, upon becoming a law, shall not be subject to veto by the governor.

Subsection (7). Either house of the General Assembly may require any person in any department, board, branch, bureau or agency of the state government to appear and be heard with respect to any budget bill during the consideration thereof, and the governor or any such person as he shall designate shall have the right to appear for the purpose of explaining the budget bill or any item therein contained.

Subsection (8). Neither house shall consider other appropriations until the budget bill has become law. Any such appropriation shall be embodied in a separate bill limited to some single work, object or purpose as clearly defined therein, and such bill shall be called a supplementary appropriation bill. Each supplementary appropriation bill, including amendments or supplements to the budget bill which have not become law, shall provide the revenue necessary to pay the appropriation by a tax, direct or indirect, to be levied and collected as shall be directed in said bill, and, in addition, in the case of amendments or supplements provided for by subsection (4) of this section, by funds available therefor in conformity with estimates made by the governor, such estimates being subject to subsection (5) of this section. No supplementary appropriation bill shall become law unless it be passed in each house by a vote of a majority of the whole number of members elected, and the yeas and nays recorded on its final passage, and such bill shall be presented to the governor as provided in Section 17

of Article 2 of the Constitution, and thereafter all of the provisions of said section shall apply. The powers and rights of the governor and the General Assembly specified in subsection (7) of this section shall apply to any supplementary appropriation bill.

Subsection (9). The General Assembly may consider any emergency appropriation at any extraordinary session.

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THIRD REPORT

OF THE

COMMITTEE ON STATE FINANCE AND TAXATION

October 24, 1966

RE: ARTICLE 14, DECLARATION OF RIGHTS; ARTICLES 15 & 43, DECLARATION OF RIGHTS; ARTICLE III, SECTION 36; ARTICLE III, SECTION 51; ARTICLE III, SECTION 37

I. ARTICLE 14, DECLARATION OF RIGHTS

The present article provides:

> That no aid, charge, tax, burthen or fees ought to be rated or levied, under any pretense, without the consent of the Legislature.

A. Background[1]

Article 14 incorporates into the Maryland Declaration of Rights the principle of "no taxation without representation" which had been expressed, for Englishmen, in the British Bill of Rights of 1689 and, for American colonists, in the Declaration of the Stamp Act Congress of 1765.

The purpose of the rule is to prevent the imposition of taxes without the consent of the elected representatives of the people. Delegations of the taxing authority to local subdivisions have been held proper, Alexander v. Mayor and City Council of Baltimore, 5 Gill

1. Much of the succeeding historical analysis of Articles 14 and 15 of the Declaration of Rights draws heavily from the excellent work of H. H. Walker Lewis, "The Tax Articles of the Maryland Declaration of Rights," 13 Md. L. Rev. 83 (1953), and from a memorandum, prepared by Mr. Lewis at the Committee's request, which brings his article to date. The Committee is grateful for Mr. Lewis' assistance.

383 (1847); Burgess v. Pue, 2 Gill 11 (1844). In some instances, however, the principle appears to have been eroded through the delegation by the legislature of taxing authority to nonelected administrative boards. Such a delegation, in unusual circumstances, was upheld in Baltimore v. State, 20 Md. 376 (1860). There, the Court of Appeals sanctioned a legislative grant of authority to a state board of police commissioners, appointed to bring to a halt widespread lawlessness and corruption in Baltimore City, to determine its own expenditures and require the city to pay them.

B. Recommendation

The Committee recommends that the article be rewritten as follows:

> *No tax shall be imposed except for a public purpose and except by the elected representatives of the people.*

The Committee believes that the historic principle of "no taxation without representation" has important modern significance in requiring that the consent of the elected representatives of the people be required before taxes can be imposed. The Committee further recommends inclusion in Article 14 of a public purpose limitation on the imposition of all taxes. The Committee believes that the public purpose test distills and applies the meaning of the last clause of present Article 15, discussed below.

II. ARTICLES 15 AND 43, DECLARATION OF RIGHTS

The present Article 15 provides:

> That the levying of taxes by the poll is grievous and oppressive, and ought to be prohibited; that paupers

ought not to be assessed for the support of the government; that the General Assembly shall, by uniform rules, provide for the separate assessment, classification and sub-classification of land, improvements on land and personal property, as it may deem proper; and all taxes thereafter provided to be levied by the State for the support of the general State Government, and by the Counties and by the City of Baltimore for their respective purposes, shall be uniform within each class or sub-class of land, improvements on land and personal property which the respective taxing powers may have directed to be subjected to the tax levy; yet fines, duties or taxes may properly and justly be imposed, or laid with a political view for the good government and benefit of the community.

The present Article 43 provides in relevant part:

> . . . The Legislature may provide that land actively devoted to farm or agricultural use shall be assessed on the basis of such use and shall not be assessed as if subdivided.

A. Background -- Article 15

1. "That the levying of taxes by the poll is grievous and oppressive and ought to be prohibited."

This clause has been changed only once, in 1864, when the word "prohibited" was substituted for the word "abolished." The tax by the "poll," or head, was at one time the only direct tax in Maryland. In a slave-holding era such taxes probably bore some rough relation to ability to pay, inasmuch as slaves were taxed by the head and their owner required to pay. The historical opposition to the poll tax apparently stems from its imposition on Maryland dissenters for the support of the Church of England. It is noteworthy that no prohibition against the poll tax appeared in the constitutions adopted in the neighboring states of Delaware, Pennsylvania and Virginia, where the poll tax was not used for support of the church. In more recent years, probably because of the association of the poll tax with the right to

vote, efforts to repeal the prohibition in the constitutional conventions of 1851, 1864 and 1867 have failed. A proposed amendment to Article 15, which included repeal of the poll tax provision, was defeated at referendum in 1890.

2. "That paupers ought not to be assessed for the support of the government."

In colonial Maryland all persons who received public alms were considered paupers and exempted from taxation. An act of the legislature in 1781 exempted from all taxation persons "whose property shall not be valued above 10 pounds current money." Pauperism is no longer defined by the General Assembly; it is arguable, however, that the general exemptions of small holdings which do currently appear in the taxing statutes are an outgrowth of the pauper exemption. Whether or not such exemptions are constitutionally mandated is open to question.

> 3. . . . that the General Assembly shall, by uniform rules, provide for the separate assessment, classification and sub-classification of land, improvements on land and personal property, as it may deem proper; and all taxes thereafter provided to be levied by the State for the support of the general State Government, and by the Counties and by the City of Baltimore for their respective purposes, shall be uniform within each class or sub-class of land, improvements on land and personal property which the respective taxing powers may have directed to be subjected to the tax levy; . . . .

As originally adopted in 1776 the clause in Article 15 directly following the pauper exemption read as follows:

> but every other person in the State ought to contribute his proportion of public taxes for the support of government according to his actual worth in real or personal property within this State.

This provision of the 1776 Declaration of Rights strongly reflects the principle of "contribution according to worth" enunciated in the same year by Adam Smith in his "Inquiry into the Nature and Causes of the Wealth of Nations." The provision has been amended three times. In 1851 the Constitutional Convention made slight changes to make it clear that nonresidents owning property in the State could be required to contribute to the support of the government and that the measure of worth was not restricted to property within the borders of the State. In 1915 an amendment passed at referendum struck out all of the existing provision requiring property taxes to be apportioned according to actual worth and substituted for it the following language:

> that the General Assembly shall, by uniform rules, provide for separate assessment of land and classification and sub-classifications of improvements on land and personal property, as it may deem proper; and all taxes thereafter provided to be levied by the State for the support of the general State Government, and by the Counties and by the City of Baltimore for their respective purposes, shall be uniform as to land within the taxing district, and uniform within the class or sub-class of improvements on land and personal property which the respective taxing powers may have directed to be subjected to the tax levy;
> . . . .

In 1960 an amendment passed at referendum brought Article 15 to its present form by permitting the classification of land for tax purposes; a development intrinsically bound up with the farmland assessment question and Article 43 of the Declaration of Rights, and discussed more fully in Section B, below.

Of all of the amendments to Article 15 by far the most significant was the classification and uniformity amendment of 1915. For years

prior to 1915, there had been considerable concern over the ease by which intangibles,such as stocks and bonds, could be hidden from the assessor and thus avoid taxation, and confusion over the permissibility of taxing intangibles,such as stocks and bonds,at reduced rates in order to place Maryland trust companies, which held large portfolios of intangibles in fiduciary capacities, in a position to compete with trust companies in other states which did not tax intangibles at the full personal property rate. An intangibles tax of 1896, providing for the taxation of income-producing securities at reduced rates,was a revenue-producing success, but was generally regarded as unconstitutional under the then existing language of Article 15. In 1915 the taxing authorities and the trust companies, aided by adherents of the single tax movement, who saw the permissibility of reduced rates for intangibles as a step toward their goal of no taxation on personal property at all, sponsored the successful campaign to amend Article 15.

Lewis points out several significant changes effected by the 1915 amendment. Among them are:

(a) A shift in emphasis from persons to property. The deleted language applied the uniformity requirement to the worth of the taxpayer; the new language applies the uniformity requirement to the assessment of, and tax on, property itself.

(b) A shift from a requirement of overall uniformity to the requirement that taxes be uniform as to land within each taxing district and as to personal property and improvements within each classification.

Lewis also points out, however, that there is no evidence suggesting that the fundamental principle of equality was intended to be abandoned. Indeed, the Court of Appeals, in Susquehanna Power Co. v. State Tax Commission, 159 Md. 334 (1930), has held that:

> Although the phrase of the Maryland Bill of Rights stating the just and salutary principle that "every person in the State, or person holding property therein, ought to contribute his proportion of public taxes for the support of the government, according to his actual worth in real or personal property," was omitted from the article -- yet it is implicit in the . . . language of the article as amended: . . . . 159 Md. at 343.

While it had long been clear that complete exemption from taxation, if the classification was reasonable, was a permissible deviation from the equality principle, see, e.g., Baltimore City v. Starr Methodist Church, 106 Md. 281 (1907); Williams v. Baltimore, 289 U.S. 36, partial exemptions from taxation, in the form of reduced assessments, were clearly authorized only by the passage of the 1915 amendment. On its face the uniformity requirement in the 1915 amendment would clearly appear to apply to both the assessment and taxation of property. For a time, however, doubt was cast on whether uniformity was constitutionally required of assessments, even within a class, by the language of the Court of Appeals in Leser v. Lowenstein, 129 Md. 244, 250 (1916), and Rogan v. County Commissioners of Calvert County, 194 Md. 299 (1950). See also 37 Op. Atty. Gen. Md. 424 (1952); Lewis, op. cit. at 103-107. The doubt has apparently been resolved in favor of the uniformity requirement, at least by way of dictum, in State Tax Commission v. Gales, 222 Md. 543, 558-559 (1960).

> 4. . . . yet fines, duties or taxes may properly and justly be imposed, or laid with a political view for the good government and benefit of the community.

The "political view" clause has been in every Maryland Constitution in substantially the same form. To the extent it authorizes the laying of taxes it is redundant since no specific authorization of the taxing power is necessary in a state constitution. Notwithstanding, some cases have referred to the clause (mistakenly, it is submitted) as the constitutional basis of indirect, non-property taxes, such as license taxes, inheritance taxes and income taxes. See, e.g., Oursler v. Tawes, 178 Md. 471, 485-486 (1940). It has also been suggested that such indirect taxes as are "authorized" by the "political view" clause are not subject to the uniformity and equality principle inherent in the preceding clauses of Article 15. See Niles, Maryland Constitutional Law, pp. 32-33. Another, rather antiquarion, reading of the "political view" clause is that it may justify the exaction of taxes not, strictly speaking, for the support of government but for the good of the community nonetheless. See, e.g., Waters v. State, 1 Gill 302 (1843), upholding a tax for the financing of the colonization of free Negroes in Africa on this theory.

B. The Agricultural Land Assessment Amendments to Articles 15 and 43

1. Legislative and Constitutional Background.

The most recent amendment to Article 15 and the amendment to Article 43 here in question are both the result of legislative efforts to secure the assessment of farmland on the basis of its use as farmland and not at its market value.

The first farm assessment bill was passed by the General Assembly in 1955. It provided that:

> Lands which are actively devoted to farm or agricultural use shall be assessed on the basis of such use, and shall not be assessed as if subdivided or on any other basis.

The bill was vetoed by the governor, passed over the governor's veto in the following year and became law on June 1, 1956. Laws of Maryland, 1956, ch. 9. The law was amended in 1957 to give the State Department of Assessments and Taxation (then the State Tax Commission) power "to establish criteria for the purposes of determining whether lands subject to assessment [under the act] are actively devoted to farm or agricultural use by the adoption of rules and regulations." Laws of Maryland, 1957, ch. 680. The criteria set forth are identical with those which presently appear in Code Article 81, § 19(b), infra.

In 1960 the Court of Appeals upheld a lower court determination that the act was unconstitutional in State Tax Commission v. Gales, supra, on the grounds that Article 15 of the Declaration of Rights, although it permitted classification and subclassification of improvements on land and personal property, did not sanction the separate classification of land for tax purposes.

In response to the Gales litigation, the 1960 General Assembly enacted two proposals for constitutional amendment. Article 15 of the Declaration of Rights was amended to read, in relevant part, as follows:

> that the General Assembly shall, by uniform rules, provide for the separate assessment, classification and sub-classification of land [and classification and sub-classifications of] , improvements on land and personal property, as it may deem proper; and all taxes thereafter provided to be levied by the State for the support of the general State Government, and by the Counties and by the City of Baltimore for their respective purposes, shall be uniform [as to land within the taxing district, and uniform] within [the] each

class or sub-class of land, improvements on land and personal property which the respective taxing powers may have directed to be subjected to the tax levy; . . . . (Brackets indicate omissions; underscoring indicates new matter.)

Article 43 of the Declaration of Rights was amended to read as follows:

> That the Legislature ought to encourage the diffusion of knowledge and virtue, the extension of a judicious system of general education, the promotion of literature, the arts, sciences, agriculture, commerce and manufactures, and the general melioration of the condition of the People. The Legislature may provide that land actively devoted to farm or agricultural use shall be assessed on the basis of such use and shall not be assessed as if sub-divided.

Both proposed amendments were ratified by the voters in the November, 1960 election by margins of nearly 3-1. Subsequently, the General Assembly re-enacted the Farm Assessment Act, Laws of Maryland, 1961, ch. 455; Maryland Code, Article 81, § 19(b), which provides:

> Lands which are actively devoted to farm or agricultural use shall be assessed on the basis of such use, and shall not be assessed as if subdivided, it being the intent of the General Assembly that the assessment of farm land shall be maintained at levels compatible with the continued use of such land for farming and shall not be adversely affected by neighboring land uses of a more intensive nature. The General Assembly hereby declares it to be in the general public interest that farming be fostered and encouraged in order to maintain a readily available source of food and dairy products close to the metropolitan areas of the State, to encourage the preservation of open space as an amenity necessary to human welfare and happiness, and to prevent the forced conversion of such open space to more intensive uses as a result of economic pressures caused by the assessment of land at a rate or level incompatible with the practical use of such land for farming. The State Department of Assessments and Taxation shall establish criteria for the purpose of determining whether lands which appear to be actively devoted to farm or agricultural use are in fact bona fide farms and qualify for assessment under this subsection. Such criteria shall be promulgated in rules and regulations which shall include, but shall not be limited to, the following:

1. Zoning applicable to the land.

2. Present and past use of the land including land under the soil bank provisions of the Agricultural Stabilization Act of the United States government.

3. Productivity of the land including timberlands and lands used for reforestation.

4. The ratio of farm or agricultural use as against other uses of the land.

Pursuant to the statutory command, the State Department of Assessments and Taxation adopted the following regulation:

Regulation No. 9

In determining whether lands which appear to be actively devoted to farm or agricultural use are in fact bona fide farms and qualify for assessment under Chapter 52 of the Acts of 1960, the following criteria shall be considered:

1. Zoning applicable to the land.
2. Applications for, and grants of, zoning reclassification in the area.
3. General character of the neighborhood.
4. Use of adjacent properties.
5. Proximity of subject property to metropolitan area and services.
6. Submission of subdivision plan for subject or adjacent property.
7. Present and past use of the land.
8. Business activity of owner on and off the subject property.
9. Principal domicile of owner and family.
10. Date of acquisition.
11. Purchase price.
12. Whether farming operation is conducted by the owner or by another for owner.
13. If conducted by another for owner, the provisions of the arrangement, written or oral, including, but not limited to, the terms, area let, consideration and provisions for termination.
14. Farming experience of owner or person conducting farming operations for owner.
15. Participation in governmental or private agricultural programs or activities.
16. Productivity of the land.
17. Acreage of crop land.

18. Acreage of other lands (wooded, idle).
19. Number of livestock or poultry (by type).
20. Acreage of each crop planted.
21. Amount of fertilizer and lime used.
22. Amount of last harvest of each crop.
23. Gross sales last year from crops, livestock and livestock products.
24. Amount of feed purchased last year.
25. Months of hired labor.
26. Uses, other than farming operation, of the land.
27. Ratio of farm or agricultural use as against other uses of land.
28. Inventory of buildings, and condition of same.
29. Inventory of machinery and equipment, and condition of same.

Section 19(b), Regulation No. 9 and, indirectly, the amendments to Articles 15 and 43 of the Declaration of Rights have recently been before the Court of Appeals in Supervisor of Assessments for Montgomery County v. Alsop, 232 Md. 188 (1963). The court there held that the grazing and feeding of a herd of more than 40 head of beef and dairy cattle on the land in question throughout the year is a "farm or agricultural use" within the meaning of the constitutional and statutory provisions. The land in question was used by a gentleman farmer who did not personally farm his land but permitted his neighbors to graze beef and cattle on his land and permitted one of his tenants to cultivate a truck garden as a sideline.

The court below, the Maryland Tax Court, had upheld the assessor's refusal to classify the land in question as a bona fide farm on the grounds:

> That the owner, seeking quiet and solitude, acquired a former farm as a country estate, and engaged in no bona fide operations;
>
> That the owner, in order to maintain the property in proper condition as economically as possible and for no

other reason, permitted a neighboring farmer to graze his cattle on the property, and to use some of the buildings thereon in return for keeping the hay cut and doing general maintenance work on and about the property, without monetary consideration;

That the owner rents the farm tenant houses to tenants at a reduced rental in order to obtain part time assistance from them in maintaining the farm and, as a matter of convenience to the owner, in tilling a small truck garden.

In reversing the Tax Court, the Court of Appeals stated:

As we see it, the question here is not whether the owner and taxpayer is personally engaged in a bona fide farm operation or is permitting a neighbor to use the land for grazing cattle without monetary consideration, but instead is whether the land is actively devoted to a "farm or agricultural use." We think it was so used.

Applying only the specified statutory standards to the facts, it appears that the land in question is zoned rural residential and that it, as well as the surrounding lands, is primarily used for farming; that the present and past use of the land is and was agricultural; that the land is used as a pasture for grazing forty or more beef and dairy cattle and for the production of hay to feed such cattle during the winter months; and that the proportion of the farm used for agricultural purposes is far in excess of the proportion used as a curtilage to the main dwelling and as yards and vegetable gardens appurtenant to the rented tenant houses. This was enough to require a finding that the land was in fact a bona fide farm, without resorting to any of the other criteria set forth in Regulation 9, some of which seem to have a limited use as a guide in determining whether or not a particular tract of land is a farm within the meaning of the constitutional and statutory provisions. In the instant case it seems clear that the grazing and feeding of a herd of more than forty head of beef and dairy cattle on the land in question throughout the year is a "farm or agricultural use" within the meaning of the constitutional and statutory provisions. . . . (Emphasis added.)

2. Testimony.

(a) State Department of Assessments and Taxation.

The Committee first considered the farmland assessment question at its meeting of March 31, 1966. Mr. Albert W. Ward,

Director of the State Department of Assessments and Taxation, and Mr. William H. Riley, Jr., State Supervisor of Assessments, were invited to present their views. Both Mr. Ward and Mr. Riley stated that they agreed with the principle that "bona fide" agricultural land should be assessed on the basis of such use and felt that the 1960 amendment to Article 15 was the only constitutional change necessary to that end. They suggested that the 1960 amendment to Article 43 not be included in the new constitution on the ground that it not only permitted but, after the Alsop decision, virtually required land which in the view of the State Department of Assessments and Taxation was not bona fide farmland to be assessed as if it were.

They reasoned as follows: The Alsop case construed the statutory standard for special assessment found in Article 81, section 19(b) -- "lands which are actively devoted to farm or agricultural use" -- as an objective test, i.e., what use is made of the land, and considered irrelevant, for example, the fact that the owner did not personally engage in farming operations. It strongly implied that a number of other criteria established by the department for determining whether land is "actively devoted to farm or agricultural use," such as the domicile of the owner and his family, the date of acquisition, the farming experience of the owner, were irrelevant to such an objective test. To Messrs. Ward and Riley, the objective test makes it impossible for them to fulfill their statutory duty under section 19(b) of establishing criteria to determine whether lands "which appear to be actively devoted to farm or agricultural use are in fact bona fide farms." The result, in their view, is to permit not only

gentleman farmers, but developers and speculators, who engage in only token farm uses, to receive a subsidy intended primarily for those whose livelihood depends on farming operations. They stated that were it not for Article 43, the results of the Alsop decision might be removed by legislative amendment of the "actively devoted" standard. In their view, however, the presence of the "actively devoted" standard in the Constitution itself means that the Alsop interpretation is of constitutional significance and raises the question of whether legislative enactment of a more flexible standard would be constitutional. In any case, Article 43 makes legislative change more difficult because it is urged on the legislators by the farming organizations as a "mandate."

Messrs. Ward and Riley stated that there have been several legislative attempts, unsuccessful to date, to write a farm assessment law which would not confer an advantage on the developer or speculator. The most recent, introduced this year, was Senate Bill 252 which would have made several important innovations in the farm assessment law:

1. Whereas the present law declares it to be in the public interest that farming be fostered to encourage a ready source of food supply close to metropolitan areas, encourage open space "as an amenity necessary to human welfare and happiness" and to prevent forced conversion of open space to more intensive uses as a result of "economic pressures caused by the assessment of land at a rate or level incompatible with the practical use of such land for farming," the only public interest stated in S.B. 252 is to encourage a ready source of food supply.

2. S.B. 252 would permit the farm assessment only to "lands actively devoted to commercial farm or agricultural use." It expressly excludes from its provisions "lands held by the owner thereof primarily for the purpose of development for any use other than active farm or agricultural use."

3. It incorporates a "deferred tax" feature which, in summary, provides that land which is assessed as commercial farmland but which also has a higher assessable value shall also receive the higher assessment and, should the farm uses of such land cease, by sale or otherwise, unpaid taxes on the difference between the farm assessment and the higher assessment, for as long as five years preceding the change or sale, may become due. A lien is imposed on the property for the taxes based on the difference between the two assessments, the so-called "deferred" taxes.

The State Department of Assessments and Taxation testified in favor of S.B. 252.

(b) Agricultural Interests.

On May 3, 1966, the Committee met with Dr. William Paul Walker, Chairman of the Department of Agricultural Economics at the University of Maryland, Mr. Young D. Hance, President of the Maryland Farm Bureau, Mr. E. Rankin Lusby, Secretary of the Maryland Farm Bureau, and Mr. Lionel Burgess of the Maryland State Grange.

All of the witnesses recommended retention of the 1960 amendments to Articles 15 and 43, although Dr. Walker indicated that the two amendments might more appropriately have been combined into one

amendment to Article 15. There was consensus among the witnesses as to the necessity that the legislature be given a "mandate" by the constitution to assess farmland at its agricultural use value and not at its market, or cash, value. Several of the witnesses, notably Dr. Walker, gave illustrations of the "non-farm use" pressures giving rise to substantial increase in the market value of farmland near metropolitan centers, among them urban expansion, increased desire for country estates, competition among neighboring farmers for land to expand in order to operate more efficiently. It was also stressed that many farmers, if forced to pay taxes on a market value assessment, could not operate profitably or would find their margin of profit so slight as to make attractive the prospect of selling their farm at a high price for development purposes. The result would be loss of farm production near urban centers, higher cost of food, and the continued loss of open space. One of the witnesses suggested that if farmland were assessed at the price for which land was acquired for Columbia, in Howard County, every farmer in the area would be out of business.

The representatives of the professional farming organizations expressed approval of the objective standard, "land actively devoted to farm or agricultural use." Although they acknowledged that token "farming" by token "farmers" might occasionally benefit speculators, they preferred such a standard to one which would permit inquiry, for example, into whether or not the land was farmed by its owner. Such a test, they pointed out, might result in market value assessment for farmland leased to a tenant farmer by a retired farmer-owner who

no longer farmed the land himself. They also expressed some apprehension at leaving substantial discretion for establishment of criteria in the tax assessment or collection officials. It was also pointed out that the present system, despite the occasional benefit to a developer or speculator, did serve a public purpose to the extent that the lower assessment reduced the pressure to subdivide and maintained open spaces.

Opposition was also expressed by the organization representatives to a deferred tax plan. Fear was expressed that a farmer who ceased active farming and sought merely to retire on his farm would be met with a prohibitive assessment at a time when he could least afford it.

Dr. Walker indicated that only two states, Maryland and New Jersey, had constitutional provisions providing for the separate assessment of farmland. Two other states, Texas and Nebraska, will vote on constitutional amendments this fall. Constitutional amendments were defeated at the polls in California and Wisconsin. Statutes providing for separate agricultural land assessment are in force in a number of states, including Indiana, Florida, New Jersey, Connecticut, Hawaii and Oregon. California and Nevada had such legislation but it was declared unconstitutional.

C. Recommendation

The Committee recommends that Article 15 be rewritten to read as follows:

No assessment nor any exemption therefrom with respect to any tax imposed in this State shall be made except pursuant to uniform rules within classes or

subclasses of taxpayers, property or events as may be provided by law, and, with respect to taxes on property, such classes may include property devoted to agricultural use.

The Committee further recommends that the language of the 1960 amendment to Article 43 be deleted from the constitution.

The Committee believes that no constitutional mandate is or ought to be necessary in order to confer on the legislature the power to tax, to assess property, to create reasonable exemptions from taxation or to make reasonable classifications of property necessary to the exercise of the taxing power. The Committee emphatically believes, however, that it is the proper office of the constitution to place such restrictions on the exercise of the legislature's taxing power as are necessary to secure the rights of Maryland citizens. In the area of taxation, the right of the citizen is to be treated uniformly with other citizens similarly situated. Indeed, it might be postulated that this is a natural right which must be protected in all events from governmental encroachment.

It is for this reason that protection from discriminatory tax practices found its way into the Bill of Rights. Present Article 15 has been interpreted by the courts to guarantee to the citizen equal and even-handed treatment in matters of property taxation. The Committee believes that this concept should be strengthened and broadened into other fields of taxation, particularly in view of the fact that in a modern society it is the excise, and

not the property tax, which extracts the greatest revenues from the people.

Uniformity in taxation does not imply universality. The core of the problem lies in proper classification. So long as proper classes are maintained, the test of uniformity will be met if all members of the class are treated alike. For these reasons, the Committee's draft mandates that classifications be established by law before a tax may be imposed. Since taxation depends upon the trilogy of the taxpayer, his or its property and the relationship of taxpayers to property -- an event -- the draft commands that the taxation process be established within these concepts.

It should be emphasized that the concept of proper classification should not be restricted solely to the property tax. Present Article 15, however, is worded in this direction. For example, it has been suggested that indirect taxes are not within the purview of Article 15. State v. P.,W.& B. R.R. Co., 45 Md. 361, 378 (1876). This decision has led one commentator to observe that the income tax is not subject to Article 15 of the Bill of Rights and that its uniformity and equality provisions are resultingly inapplicable. Cairns,"History and Constitutionality of the Maryland Income Tax Law," 2 Md. L. Rev. 1 (1937).

Uniform treatment in matters of taxation does not, however, depend solely on proper classification. Classification properly made is but the first step. The necessary corollary is that each class or subclass which defines the incidents of taxation must be treated by uniform rules. Thus, the objective standards that fix the tax

burden must be equally applied to each incident of a similar nature. The Committee recognizes this mandate by requiring that all assessments and exemptions within a recognized class shall be made "pursuant to uniform rules."

The test of "uniform rules" will achieve complete uniformity within recognized classifications if the tax is indirect. Thus, two persons with the same net taxable income will pay the same income tax -- assuming they enjoy the same degree of exemptions, a subject discussed below. This is not true, however, in the field of direct taxation in which the assessment procedure depends not entirely upon objective, discernible facts but to some extent upon subjective judgments of the assessor. For this reason, the courts have long recognized and enunciated the postulate that complete uniformity in property taxation is unobtainable. The Committee recognizes and accepts this proposition. The mandate of "uniform rules," however, will achieve as close an approximation to uniformity in property taxation as is humanly possible under our present system.

The direct burden of any tax is imposed through the process of assessment, whether the tax be direct or indirect. The indirect burden of taxation, however, is derived not by what the individual taxpayer must pay by reason of his assessment but, rather, by what his neighbor does not pay because of his underassessment. The concept is, in the last analysis, one of distribution. If the common government requires a sum certain to operate, the entire citizenry must pay the bill. An underassessment requires a shifting of the burden which may or may not be fair depending upon the method by which the burden is distributed.

The most common cause for underassessment in the broad, generic sense is the exemption from taxation. Exemptions are of many kinds are are the product of many motives -- social, economic, political. Exemptions from tax may, therefore, be justified on sound grounds; they may also be subject to strong critique. But one point remains clear -- exemptions from taxation should not be allowed unless they are imposed "by uniform rules."

It is not the province of this Committee to judge whether the many exemptions which currently erode the Maryland tax system are good or bad. The Committee does recognize, however, that exemptions in the area of direct taxation are not uniform in this State. Article 81, section 9, of the Annotated Code of Maryland (1965 Replacement Volume) contains no less than sixty exemptions from the property tax. Thus, real property owned by Nature Conservancy, Inc., in Calvert County is exempt from tax; similar property located elsewhere, if any, is not. Again, the property of Arts, Easton, Maryland, is exempt with qualifications; union-owned property in Allegany County is selected for favor; the property of the Frederick Optimist Boys' Foundation, Inc., or part of it, pays no tax. The examples could be multiplied. Suffice it to say that taxpayers in many parts of the State do enjoy special privileges in tax matters at the expense of the general citizenry who do not.

The Committee believes that all exemptions -- like all assessments -- should be granted uniformly throughout the State. To meet this point, the Committee proposes that exemption from tax shall be made pursuant to uniform rules. No comparable provision is to be

found in the existing Constitution. However, the recommendation has found favor with all state tax administrators with whom the Committee consulted.

The proposed draft represents an attempt on the part of the Committee to place the concepts of uniform and fair tax practice in the constitution in broad and meaningful fashion. The requirements in the draft will apply to all taxes and all exemptions from taxes. Additionally, the Committee's proposal will apply to every legislative body in Maryland that imposes a tax.

The draft makes special mention of the permissibility of the separate classification of farmland. The Committee recognizes that inclusion in the provision as redrafted of this special form of sub-classification of land is not essential in order for the legislature to possess the classification power; the Committee feels, however, that in view of the very recent adoption at referendum, by an overwhelming majority of the voters, of the amendments to Articles 15 and 43 favoring the special farmland assessment, an explicit sanction of the farmland assessment would be an appropriate expression of the public policy of the State. It will be noted, however, that the language relating to the farmland assessment is general and does not include the "actively devoted" test currently embodied in Article 43. The Committee believes, in view of the many possible assessment standards discussed earlier in this report, each reflecting different policy considerations on the farmland assessment question, that these considerations ought not be reconciled in

our organic law. The Committee desired to place in the legislature responsibility for choosing among the competing policy considerations in this important area.

The Committee did not consider that retention of the abolition of the poll tax was necessary. Stripped of its applicability to voting rights,[2] the Committee saw no objection to such a capitation tax if it met the test of uniformity required by the proposed article and the due process and equal protection tests proposed for inclusion elsewhere in the Declaration of Rights.

The Committee recommends abolition of the "paupers" clause on the ground that its significance is historical only and that it has no modern meaning.

The Committee further recommends abolition of the "political view" clause. In the Committee's view the essential meaning of the clause has been given expression in the first clause of the proposed draft of Article 14.

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2. In Harper v. Virginia State Board of Elections, 86 S. Ct. 1079 (1966), the Supreme Court held payment of poll taxes as a voting requirement unconstitutional. It said nothing to impair the poll tax as such "so long as it is not made a condition to the exercise of the franchise." 86 S. Ct. at 1082.

III. ARTICLE III, SECTION 36 -- THE LOTTERY

Article III, Section 36 of the present Constitution reads as follows:

> No lottery grant shall ever hereafter be authorized by the General Assembly.

The Committee recommends that no such prohibition be included in the new constitution.

A. Background

It will surprise many Marylanders to learn the substantial extent to which various forms of lottery helped to finance some of the more venerable of our institutions. According to a list published by the Commissioners of Lotteries in 1818, lottery schemes had helped raise funds for the construction of the churches and cathedrals of a number of different faiths, hospitals, monuments, roads, libraries and schools. It has been estimated that from 1791 to 1800 approximately 180 lottery grants and their extensions produced some 3,200 lotteries in the City of Baltimore alone, attracting $180 million, of which $120 million was returned as prize money and $60 million divided among the promoters, the State and the intended specific beneficiaries of the lottery schemes. A Board of Lottery Commissioners was established in 1818 to supervise and tax all lottery grants in the State. In practice, the schemes did not raise funds either quickly or easily for the intended projects. In order that the Maryland lotteries be competitive with lotteries in other states, it was often necessary to return in prize money most of the money collected with only a small percentage retained for the construction project to be

assisted. Thus, many extensions of lottery authorizations were essential before the intended projects were complete. By the 1830's substantial sentiment existed for the curbing and eventual abolition of the lottery grants on the grounds that they were a slow and economical system for the raising of funds for public and quasi-public projects, created pauperism, and were marked by mismanagement and even corruption on the part of the commissioners. See Report on Legalized Gambling (Baltimore Criminal Justice Commission, 1964) pp. 3-7, 23-35.

The present constitutional prohibition was adopted, after heated debate, in the convention of 1851. It will be noted that it prohibits future lottery grants. It was not until 1860 that the legislature finally abolished all lotteries then existing within the State.

The point was raised in testimony before the Committee that the constitutional prohibition against "lottery grants" might be construed to bar only grants by the legislature of authority to private corporations or individuals to operate a lottery but not to prevent the institution of a state-operated lottery. In this connection, an opinion of former Attorney General Herbert R. O'Conor, written in 1935, is relevant. The question before the attorney general was the constitutionality of proposed legislation which would have authorized the operation by the State of a sweepstakes on horse racing in Maryland. After deciding that a sweepstake was a "lottery" as that term is used in Section 36, the attorney general went on to say:

> As far as I am informed, since the incorporation of Section 36 in Article III of our Constitution in 1841, our Legislature has not attempted to authorize the operation of a lottery by the State,

> or by any other agency, and there is no case since its incorporation in the Constitution which decides that the prohibition operates equally against the right of the Legislature to authorize a lottery to be run by the State as well as by an individual. However, in the case of Lucas, et al, vs. McBlair, 12 G & J, page 1, it clearly appears from the opinion that the effect of the Constitutional Amendment was to prevent the operation of lotteries in this State, subsequent to the date of its enactment.
>
> I am of the opinion, therefore, that . . . [the bill] is unconstitutional . . . . 20 Op. Atty. Gen. Md. 266 (1935).

TESTIMONY

The Committee took testimony on the lottery question on August 15, 1966. It invited Hyman Pressman, Comptroller of the City of Baltimore, an exponent of abolition of the present provision and an advocate of a state-operated lottery, and over a dozen religious leaders. In addition to Mr. Pressman, only Roy D. Gresham, Executive Secretary of the Baptist Convention of Maryland, and Harry Mills, Executive Director of the Division of Christian Social Relations for the Episcopal Diocese of Maryland, appeared to testify. The Committee also received a written communication from Francis X. Gallagher, Esq., counsel to the Roman Catholic Archdiocese of Maryland.

Mr. Pressman favored abolition of the existing provision on numerous grounds: (a) it is inconsistent to bar lotteries but not pari-mutual betting at race tracks, (b) a state-operated lottery would take from organized crime a major source of revenue, namely, the numbers racket, (c) a state-operated lottery would raise money for sound public purposes, and (d) most citizens favor a state-operated lottery and their will should not be thwarted. Mr. Mills presented

a statement of the Right Reverend Harry Lee Doll, Bishop of Maryland, favoring retention of the present prohibition on the grounds that the lottery is immoral, corrupts the young by its sanction of "easy money," would be an admission that our taxpayers will not support their government and would "open the flood gates of crime." Mr. Gresham also favored retention of Section 36 on the grounds that gambling is a destructive, parasitic force in society and that the lottery would bring in its wake crime and poverty. Mr. Gallagher's letter to the Committee expressed no opinion on the merits of a state-operated lottery but suggested that the question was properly one for legislative determination "and not the type of subject matter which should be included in a state constitution." Mr. Gallagher stated that Cardinal Shehan concurred in this view.

B. Recommendation

In recommending against retention of the present prohibition, the Committee in noway wants to be understood as favoring the adoption of a state-operated lottery or any other form of gambling device for the alleged purpose of raising revenue for the State. The Committee's recommendation is based on its conviction that the issue is not of such dimension as should be treated in the State's organic law. While impressed with the persuasive arguments against the wisdom of a state-operated lottery, the Committee feels that these arguments should be addressed to the elected representatives of the people. The Committee is also aware of the fact that the constitutions of at least 35 other states bar or sharply restrict lottery operations. The Committee believes, however, that the elements of the lottery question, important

and far-reaching as they may be, do not sufficiently touch the fundamental questions of the relationship of the citizen to the State and of the apportionment of power within the State which, in the Committee's judgment, ought to be the exclusive subjects of constitutional import.

IV. ARTICLE III, SECTION 51

A. Background

The section reads as follows:

> The personal property of residents of this State, shall be subject to taxation in the County or City where the resident bona fide resides for the greater part of the year for which the tax may or shall be levied, and not elsewhere, except goods and chattels permanently located, which shall be taxed in the City or County where they are so located, but the General Assembly may by law provide for the taxation of mortgages upon property in this State and the debts secured thereby, in the County or City where such property is situated.

The section came into the Constitution in the convention of 1867 over strong objection that the subject matter was more appropriate for legislative determination. Proponents of the constitutional provision argued that it was necessary in order to prevent wealthy Baltimoreans, who resided in the city but had country homes in the county, from continuing to escape city taxation as existing legislation apparently permitted them to do. The sharp language of the debate has relevance today; indeed, its echoes were heard at the last session of the legislature.

> Mr. Barry [an opponent of the proposed provision] said the whole thing was a blow at Baltimore County, and the argument of the gentleman from Baltimore (Mr. Brown), that it was for

the benefit of the State was fallacious. These gentlemen wanted to make the citizens who betook themselves to the more congenial clime of Baltimore County pay for their police, their fire department, and their Druid Hill Park, which was born of corruption and festering in corruption. The citizens of Baltimore County did not jump over the lines into other counties because the taxes might be less than in their county. They did not do anything of this kind. These gentlemen whom it was desired to strike at voted in Baltimore County, and a man's residence was certainly where he voted.

Mr. Gill thought this objection came with a bad grace from Baltimore County. The gentlemen who come into the city make their money there, and receive all the benefits of the City of Baltimore, should surely not object to pay their proportion of the taxes. He knew of two gentlemen who lived side by side, one of whom claimed his residence in Frederick County, although there only for a month or two, and the difference in taxation enabled him to pay all the expenses of his country residence. Did these wealthy citizens really live in the counties? No, it was only a part of the scheme to escape city taxation. Look how they were burdened now by the taxes imposed on them by the irresponsible parties in power.

Mr. Barry desired to know why the since [sic] of the peculating officials of Baltimore City should be visited on Baltimore County. What had Baltimore County to do with the almshouse corruptions, the Druid Hill Park, or any other villainy in the City of Baltimore. They were willing to receive any one who came among them and behaved himself as a good citizen should.

Mr. McKaig said the practice of these wealthy citizens of Baltimore, who received all the benefits of the city protection, in going into the counties to escape taxation, was a base subterfuge, and unworthy of a gentleman.

Mr. Buchanan said the gentleman from Allegany had charged gentlemen who, to his knowledge, had been citizens of Baltimore County for years with committing fraud upon the City of Baltimore and being liars. Such language as this, coming from a member of this Convention, was, to say the least, uncalled for and undignified. Baltimore County was no beggar from Baltimore City. She wanted

> nothing that was not her right, and that she would have at all hazards. Baltimore County had no hostility to Baltimore City; she sympathized with the city in her troubles, and the manner in which she was being plundered, but they were willing to meet them on this section before the Legislature and asked that it be struck out. . . . Perlman's Debates of Maryland Constitutional Convention of 1867, pp. 288-290.

The convention adopted the section by a vote of 44 to 23. The last clause of the present section, relating to the taxation of mortgages, was included in the section by virtue of its adoption at referendum in 1891.

The interpretation of the section by the courts has, for the most part, not been noteworthy, most of the litigation involving disputes over the applicability of the language of the section to particular kinds of property and interests in property. See, e.g., Kinehart v. Howard, 90 Md. 1 (1899)(stocks and bonds held by guardian in Washington, D. C., not taxable in Harford County even though husband of ward, holding equitable interest in property, was Harford County resident); Baldwin v. Washington County, 85 Md. 145 (1897) (stocks held by guardian appointed under will probated in Washington County, domicile of deceased, taxable in Washington County even though guardian and ward were residents of New York); Hopkins v. Baker, 78 Md. 363 (1894) (floating stock of partnership); McLane v. State Tax Comm., 156 Md. 133 (1928) (intangible partnership property). Although one act of the General Assembly has been declared unconstitutional as an attempt to alter the situs rule set forth in the section, Baltimore v. Alleghany County, 99 Md. 1 (1904) (act granting Alleghany County all local taxes on stock of corporations created within county, no matter

where owners of shares reside, invalid), the section has been construed to permit the legislature to significantly affect the situs rule. See, e.g., McLane v. State Tax Comm., supra (legislative determination that partnership is distinct legal entity held not in conflict with Section 51); Baltimore City v. Safe Dep. & Trust Co., 97 Md. 659 (1903) (legislative determination that, for tax purposes, property held in trust is to be treated as belonging to beneficial owner, upheld). The substance of the constitutional requirements, as construed by the courts, is codified in Article 81, § 8 of the Maryland Code.

B. Recommendation

The Committee recommends that Article III, Section 51 be deleted. The Committee believes that the determination of where property should be taxed should be for the legislature, subject to the restrictions of the due process clause and to the uniformity rule of proposed Article 15 of the Declaration of Rights, where applicable. A constitution is too blunt an instrument with which to draw the fine lines necessary in this aspect of the field of taxation. Furthermore, in the Committee's view, the situs question is intimately related to the present legislative reevaluation of the several sources of tax revenue and their allocation among the various subdivisions. The Committee feels this is an additional reason to leave the situs question to legislative determination.

V. ARTICLE III, SECTION 37

The present section provides:

> The General Assembly shall pass no Law providing for payment by this State, for Slaves emancipated from servitude in this State; but they shall adopt such measures, as they may deem expedient, to obtain from the United States, compensation for such Slaves, and to receive, and distribute the same, equitably, to the persons entitled.

The Committee recommends deletion of the section.

Respectfully submitted,

Committee on State Finance and Taxation

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